

IN THE ARBITRATION UNDER CHAPTER 11  
OF THE NORTH AMERICAN FREE TRADE AGREEMENT  
AND UNDER THE UNCITRAL ARBITRATION RULES  
BETWEEN

- - - - - - - - - - -x  
:  
METHANEX CORPORATION,                   :  
:  
                  Claimant/Investor,       :  
:  
          and                               :  
:  
UNITED STATES OF AMERICA,               :  
:  
                  Respondent/Party.       :  
:  
- - - - - - - - - - -x   Volume 7

Wednesday, June 16, 2004

The World Bank  
1818 H Street, N.W.  
MC Building  
Conference Room 13-121  
Washington, D.C.

The hearing in the above-entitled matter  
came on, pursuant to notice, at 1:35 p.m. before:

V.V. VEEDER, Q.C., President

PROF. W. MICHAEL REISMAN, Arbitrator

J. WILLIAM ROWLEY, Q.C., Arbitrator

Also Present:

SAMUEL WORDSWORTH,  
Tribunal Legal Secretary

MARGRETE STEVENS,  
Senior ICSID Counsel  
Tribunal Administrative Secretary

Court Reporter:

DAVID A. KASDAN, RDR-CRR  
Miller Reporting Company, Inc.  
735 8th Street, S.E.  
Washington, D.C. 20003  
(202) 546-6666

APPEARANCES:

On behalf of the Claimant/Investor:

CHRISTOPHER F. DUGAN, ESQ.  
CLAUDIA CALLAWAY, ESQ.  
ALEXANDER W. KOFF, ESQ.  
SABRINA ROSE SMITH, ESQ.  
MATTHEW S. DUNNE, ESQ.  
Paul Hastings Janofsky & Walker, L.L.P.  
10th Floor  
1299 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004-2400  
(202) 508-9500  
alexanderkoff@paulhastings.com

APPEARANCES: (Continued)

On behalf of the Respondent/Party:

WILLIAM H. TAFT, IV, ESQ.

Legal Adviser

RONALD J. BETTAUER, ESQ.

Deputy Legal Adviser

MARK A. CLODFELTER, ESQ.

Assistant Legal Adviser for International  
Claims and Investment Disputes

BARTON LEGUM, ESQ.

Chief, NAFTA Arbitration Division, Office  
of International Claims and Investment  
Disputes

ANDREA J. MENAKER, ESQ.

DAVID A. PAWLAK, ESQ.

JENNIFER I. TOOLE, ESQ.

CARRIELYN GUYMON, ESQ.

MARK S. McNEILL, ESQ.

Attorney-Advisers, Office of  
International Claims and Investment  
Disputes

Office of the Legal Adviser

U.S. Department of State

Suite 203, South Building

2430 E Street, N.W.

Washington, D.C. 20037-2800

(202) 776-8443

legumbc@state.gov

1776

C O N T E N T S

PAGE

CLOSING ARGUMENT

For Methanex Corporation: Mr. Dugan

1777

1 P R O C E E D I N G S

2 PRESIDENT VEEDER: Good afternoon, ladies  
3 and gentlemen. We start day eight of this hearing.  
4 And we now hear Methanex's closing oral  
5 submissions.

6 Mr. Dugan, the floor is yours.

7 CLOSING ARGUMENT BY COUNSEL FOR CLAIMANT/INVESTOR

8 MR. DUGAN: Thank you very much.

9 Members of the Tribunal, I'd like to start  
10 off with the question of what is the appropriate  
11 test here, and that will include the motion to  
12 reconsider, and the first issue I'd like to draw  
13 the Tribunal's attention to is the letter that we  
14 sent to the Tribunal on June 13th, in which we  
15 pointed out that the California regulation that we  
16 have been--that we have identified as one of the  
17 measures in this case does, in fact, ban methanol  
18 by name.

19 Now, I think you all have seen the letter,  
20 and it says that covered ox--I will wait for the  
21 Tribunal.

1 (Pause.)

2 MR. DUGAN: Now, if I could direct your  
3 attention to the second to the last page of the  
4 letter, that includes the operative language of the  
5 regulation as it exists today, and on the--I'm  
6 sorry, of the exhibits to the letter. Yes, that's  
7 it.

8 And if you look at the left-hand column,  
9 number four, it says, covered oxygenates. Oxygen  
10 from the following oxygenates is covered by the  
11 prohibitions in Section 2262(6)(C)(1), (2), and  
12 (3), and then, of course, it lists methanol as the  
13 first one, along with some of the other familiar  
14 oxygenates that we have seen in the list from the  
15 EPA and from Mr. Caldwell. At the very end is  
16 TAME, there's also DIPE, ET, BE. So, it quite  
17 specifically bans methanol in its use as an  
18 oxygenate.

19 And one other point to make: It  
20 specifically identifies methanol as an oxygenate.

21 PRESIDENT VEEDER: Mr. Dugan, just as a

1 matter of paperwork, to what extent does this  
2 enclosure differ from the actual regulations you  
3 handed out last Monday in your opening oral  
4 submissions when you added a document to Tab 41?

5 MR. DUGAN: It should be identical. It  
6 should be identical. It's just a different format.  
7 This one was printed out on the computer. I think  
8 the other one was copied, actually, from the book  
9 of California regulations. But I don't have--I may  
10 be wrong, but I have no reason to believe that they  
11 are different.

12 Now, the issue of whether or not the  
13 California regulations banned all oxygenates other  
14 than ethanol, Methanex raised over two years ago.  
15 In its First Amended Claim on February 12th, 2002,  
16 it expressly said that one of the measures that it  
17 was complaining of at that time, before the  
18 amendment was formally granted, was that--I'm  
19 referring now to page eight, paragraph 22 of the  
20 Draft Amended Claim of February 12, 2001. The  
21 second measure that Methanex challenges is the set

1 of California or CaRFG3 regulation adopted by CaFRB  
2 on September 2nd, 2000 which implemented Executive  
3 Order D 599. In implementing Governor Davis's  
4 Executive Order, the CaRFG3 regulations prohibited  
5 the use of MTBE as of December 31st, 2002, and  
6 facilitated its accelerated removal from all  
7 California gasoline prior to that date.

8           The regulations, and I'm skipping the word  
9 CaRFG3 because it doesn't lend itself to an easy  
10 acronym, went beyond merely banning MTBE, however.  
11 They also provided that only methanol, which is  
12 almost entirely a domestic product, could be used as  
13 an oxygenate in California gasoline. Consequently,  
14 the regulations ban not only MTBE, but methanol as  
15 well, from competing with methanol in the  
16 California oxygenate market.

17           Now, the difference between the  
18 regulations as they existed in proposed form in  
19 February of 2002, and the regulations as they exist  
20 now, is that now California has specifically named  
21 methanol as one of the banned substances.

1           PRESIDENT VEEDER: Mr. Dugan, would it be  
2 helpful if we just came to the point that concerns  
3 the Tribunal, and it's really a clarification of  
4 your case. Are you relying upon either the  
5 proposed regulations, which you exhibited to the  
6 legal authorities to your Amended Statement of  
7 Claim, or the actual regulations which came into  
8 effect in May of 2003, which you gave to us on day  
9 one of this hearing, as separate measures which you  
10 attack, or do you rely upon these documents as  
11 evidence in your attack on the two measures which  
12 you originally pleaded in the Amended Statement of  
13 Claim; namely, the Executive Order and the  
14 California regulations before they expressly  
15 mentioned methanol?

16           MR. DUGAN: Well, the California  
17 regulations that we included with the Second  
18 Amended Claim actually include this very language.

19           PRESIDENT VEEDER: Well, they weren't  
20 regulations. They were proposed regulations.

21           MR. DUGAN: Correct. They were proposed

1 regulations that were adopted I think two months  
2 after we filed the claim.

3           So, I mean, if the--we certainly are  
4 relying on the regulations as they exist now in  
5 banning methanol.

6           PRESIDENT VEEDER: But what form? Is it  
7 evidence of your existing case or development of  
8 your case?

9           MR. DUGAN: No, no. It's a development of  
10 the case. This is obviously an amendment by  
11 California that took place after we filed our  
12 Second Amended Claim, and we assert that it's  
13 relevant for the obvious purpose. We go back to  
14 what the Tribunal was concerned about two years  
15 ago, and that was the fact that the ban did not  
16 identify methanol, and because it did not expressly  
17 name methanol as one of the banned substances, the  
18 Tribunal set up this test in order to determine  
19 whether it was a legally significant relationship  
20 that would meet the requirements of relating to.

21           Well now, the measure, the very measure

1 that we complain of, as amended, bans methanol, and  
2 so, yes, we rely on the measure as amended after we  
3 filed our Second Amended Complaint.

4 Now, if it's necessary for us to amend our  
5 complaint yet again to rely upon the language that  
6 we included in the Second Amended Complaint that  
7 was subsequently adopted by California in, I  
8 believe, May of 2003, eight or nine months after we  
9 put it in, and which goes into effect I think in  
10 January of this year, then we move to amend the  
11 complaint because of a subsequent amendment of the  
12 regulations after our Second Amended Claim was put  
13 in.

14 Now, I'm not sure that's  
15 necessarily--that's actually necessary because it's  
16 the same measure that we are complaining of, and  
17 it's the same legal effect that we are complaining  
18 of; namely, the banning of everything except  
19 ethanol.

20 The only difference is is that now the  
21 express itemization of methanol has, in fact,

1   become a regulation.

2               Now, if an amendment is necessary, I don't  
3   think--there is no reason in Methanex's mind why it  
4   should be denied. There's certainly been no  
5   prejudice to the United States. They briefed every  
6   single argument.

7               PRESIDENT VEEDER: Just take it very  
8   slowly in stages because we are trying to see  
9   whether it goes to evidence, where obviously there  
10   is an argument for a ruling evidential case, or  
11   whether it's an additional measure or an addition  
12   to an existing measure which is subject to  
13   criticism.

14              And if you have referred to paragraph 22,  
15   if you could turn to that, it's page eight of your  
16   Amended Statement of Claim, if you can just go  
17   through the language of that to see to what extent  
18   the May 2003 regulations fit into that language.  
19   It's paragraph 22, page eight, of Methanex's  
20   Amended Statement of Claim.

21              You see you there identify the second

1 measure that Methanex challenges is the set of Cal  
2 Reg 3 regulations adopted by CAFRB on September the  
3 2nd, 2000.

4 Now, if you at this date, namely the 5th  
5 of November, 2002, identify what those regulations  
6 were, they will be the regulations which did not  
7 expressly mention methanol; would that be right?

8 MR. DUGAN: That would be right because at  
9 that time, obviously, we didn't have any  
10 regulations that expressly banned methanol. They  
11 weren't--

12 PRESIDENT VEEDER: But what you say is  
13 that those regulations implicitly banned methanol  
14 because they provided that only ethanol could be  
15 used as an oxygenate in California gasoline.

16 MR. DUGAN: Right. I don't think they  
17 implicitly. I think--they certainly didn't  
18 expressly methanol qua methanol, but I think they  
19 expressly banned all alcohols other than ethanol.

20 PRESIDENT VEEDER: Well, I'm looking at  
21 the last sentence.

1           MR. DUGAN: Correct, consequently the  
2 regulations ban not only MTBE, but methanol as well  
3 from competing with ethanol in the California  
4 oxygenate market.

5           I think the regulations had the same legal  
6 effect as far as the ban on methanol at that time.  
7 Methanol was not allowed to compete with ethanol at  
8 that time. So, the legal effect of the regulations  
9 was the same. The difference now is that the  
10 regulation, as amended, in more detail expresses  
11 exactly what the effect of the ban is, which is to  
12 ban methanol.

13           Now, we've always complained of a  
14 California measure that bans methanol, not just  
15 MTBE, but bans methanol as a competitor to ethanol.  
16 And we have consistently done that since we first  
17 put in our amended claim in February of 2002. The  
18 change here is that California has amended its  
19 regulations subsequent to our last amended claim of  
20 October 2002 to expressly name methanol.

21           PRESIDENT VEEDER: Mr. Dugan, if I can

1 just come to the point that troubles the Tribunal,  
2 if it's part of a rolling evidential case, subject  
3 to failure of the United States, you are probably  
4 pushing at an opened door. If it's a modification  
5 or an amendment of your previous case, heading the  
6 May 2003 Cal regs as a new measure subject to  
7 attack, particularly for the purpose of 1101, then  
8 I think you've got to help us on jurisdiction,  
9 power, and discretion to allow that amendment, as  
10 we understand it because that is and will still be  
11 opposed by the United States.

12 MR. DUGAN: I understand that, and  
13 obviously I think, then, you know, perhaps we are  
14 relying on it for two purposes, if I could state  
15 for the record. For the second, we are clearly  
16 relying upon it as evidence of--and we would say  
17 conclusive evidence--of California's intent to harm  
18 methanol producers and to ban methanol and harm all  
19 methanol producers, including foreign medical  
20 producers.

21 Secondly, in terms of whether an amendment

1 should be allowed to put this specific measure in,  
2 we think quite clearly it should. Number one, the  
3 UNCITRAL regulations create, I believe, a  
4 presumption that amendment can be made, so long as  
5 there is no undue prejudice. We think we fit  
6 squarely within that presumption.

7           The amendment, the regulation amendment  
8 that we are pointing to, was adopted by California  
9 well after we put in our amended claim. We noted  
10 in the amended claim that we included the proposed  
11 regulations that were actually going to be adopted  
12 naming methanol. So, as of October 2002, we had  
13 done everything that we could.

14           Now, the regulations were subsequently  
15 adopted. They did, in fact, name methanol, so it  
16 was an amended regulation.

17           Remember, the regulations are what we've  
18 always posited as the measure that we are  
19 complaining of, the CaFRB regulations, and this is  
20 just the latest iteration of the CaFRB regulations.

21           But, if an amendment is required, again, I

1 think the presumption is we are entitled to amend  
2 unless there is a showing of prejudice, and I can't  
3 see what showing prejudice there is for the United  
4 States, since they briefed and argued at length, as  
5 the Tribunal knows well, every single argument in  
6 this case.

7           And it obviously prejudices them in the  
8 sense that I think it takes away any possible case  
9 for arguing that the specific intent to harm test  
10 should be applied, but that's obviously a  
11 substantive consequence that's not within the scope  
12 of a reason why an amendment should not be allowed.  
13 So, if an amendment is necessary, and I don't think  
14 it is, but if an amendment is necessary, then, yes,  
15 we formally move to amend it, and we ask the  
16 Tribunal to consider what prejudice there is to the  
17 United States, especially given the fact that this  
18 amended regulation was amended after we filed our  
19 last amended complaint.

20           PRESIDENT VEEDER: Another possible  
21 complication is not Article XX alone, but also the

1 scope of the dispositive in our Partial Award.

2 Would you like to address us on that.

3 MR. DUGAN: I'm not quite sure what you're  
4 referring to.

5 PRESIDENT VEEDER: If you refer to--if you  
6 can refer to the Partial Award, and if we can start  
7 with the dispositive at the very end, it's page 74,  
8 paragraphs four and five.

9 MR. DUGAN: I'm sorry, I must have a  
10 differently paginated version.

11 PRESIDENT VEEDER: It's Chapter M, 102.  
12 If you go to paragraph 172, if you start with  
13 subparagraph three, and then turn to four.

14 MR. DUGAN: Yes, I see that. I guess our  
15 response would be that this is overtaken by  
16 subsequent facts.

17 PRESIDENT VEEDER: Just to complete the  
18 reference, turn back to 162, which is page 68 of  
19 our pagination.

20 MR. DUGAN: Paragraph 162?

21 PRESIDENT VEEDER: Paragraph 162, which is

1 page 68. And if you turn to line six, The fresh  
2 pleading must not exceed the limits of Methanex's  
3 existing case, pleaded and unpleaded. That's  
4 reference to the oral argument that you advanced on  
5 jurisdictional hearing.

6 MR. DUGAN: Correct. Um-hmm.

7 PRESIDENT VEEDER: We do not intend  
8 Methanex to make any new claim in its fresh  
9 pleading and so on.

10 MR. DUGAN: And I don't think we did.  
11 Remember, that's why I pointed back to what we  
12 filed in February of 2001, before this came out.  
13 We argued in 2001 in our First Amended Claim that  
14 what California had done was to ban all competing  
15 alcohols, including methanol from competing with  
16 ethanol.

17 So, we made the same claim in the February  
18 2001 First Amended Claim as we made in the Second  
19 Amended Claim.

20 So, I don't think the Second Amended Claim  
21 went beyond what was in the First Amended Claim in

1 any way.

2           And I think--the reason why I don't think  
3 an amendment is necessary is I think the operative  
4 legal effect of these various measures has been the  
5 same in their various amended forms. And their  
6 operative legal effect is to ban all competitors to  
7 ethanol. That's what we alleged in February of  
8 2001, and that's what we allege now. The  
9 difference, of course, is that there has been a  
10 specific amendment to this expressly name methanol,  
11 and that's been adopted and come into force.

12           ARBITRATOR REISMAN: Mr. Dugan, perhaps  
13 you could help me, since I was not part of the  
14 Tribunal for the rendering of the Partial Award.

15           Didn't the RFG2 say that other oxygenates  
16 could not be used until a multimedia study was  
17 conducted and RFG3 simply indicates which other  
18 oxygenates have not yet been the subject of the  
19 multimedia study.

20           MR. DUGAN: No, I would agree that is  
21 correct. And it's what the--

1           ARBITRATOR REISMAN: My next question then  
2 goes to the substantive implication, if in the  
3 Partial Award the Tribunal was unable to get over  
4 1101 on the basis of something that was implicit,  
5 why would it get over Article 1101 now when  
6 subsection four simply makes explicit what was  
7 already available to the Tribunal at the time of  
8 the Partial Award?

9           MR. DUGAN: Because the way I read the  
10 Partial Award, the Partial Award couldn't get over  
11 1101 because methanol was not expressly named. And  
12 I think that's referred to a number of times in the  
13 Award as one of the principal bases, principal  
14 bases why the measure did not, on its face, meet  
15 the relating-to requirement because it didn't name  
16 methanol.

17           Now, obviously that has now changed, and I  
18 don't think it was a question of whether it was--in  
19 fact, I would go so far as to say that the Tribunal  
20 implicitly rejected our argument that the  
21 California regs implicitly banned methanol and

1 required an express naming in order to meet the  
2 relating-to test on a per se basis. And now we  
3 have that.

4 ARBITRATOR ROWLEY: Mr. Dugan, if you  
5 could turn with me to paragraph 33 of the Partial  
6 Award, if you have it handy, and if not, I will  
7 read it to you.

8 MR. DUGAN: Paragraph 33?

9 ARBITRATOR ROWLEY: Yes, paragraph 33.

10 MR. DUGAN: Yes, I have it.

11 ARBITRATOR ROWLEY: And you will see there  
12 is a bolded subtitle of the California regulations,  
13 and if you drop down to the fourth, last line in  
14 the middle, and there is a reference to several of  
15 the earlier California reformulated gasoline  
16 regulations, but in the fourth line it says, in  
17 particular, subsection 2262.6 provided at  
18 Subsection A 1 that starting in December 31, 2002,  
19 and it reads on.

20 Now, as I understand it, that regulation  
21 was referred to in your Draft Amended Claim

1 because, if you look at paragraph 32, we say the  
2 U.S. measures, and I emphasize that, the U.S.  
3 measures, our language, for the purposes of Article  
4 1101, NAFTA, as alleged in the Amended Statement of  
5 Claim, and actually it was a draft Amended  
6 Statement of Claim, are the California Executive  
7 Order described above and the CFRFG3 regulations  
8 described below.

9           So assuming that we are right on that,  
10 that in your draft Amended Statement of Claim you  
11 referred to, 2262(6), that was a regulation which  
12 you said was a measure under attack as falling foul  
13 of Chapter 11.

14           MR. DUGAN: Correct.

15           ARBITRATOR ROWLEY: Now, that measure did  
16 not mention methanol specifically.

17           MR. DUGAN: Correct.

18           ARBITRATOR ROWLEY: You now, and the  
19 President has read you the language of our order  
20 found at paragraph 162 which says, We do not intend  
21 Methanex to make any new claims, and it must not

1 exceed the limits of Methanex's existing case  
2 pleaded and unpleaded.

3           What we now understand you to say is that  
4 you are attacking as a measure the California  
5 regulation, albeit of the same number which has  
6 recently been amended to name methanol, and I  
7 suppose will be argued by the United States that  
8 that is, indeed, because it has been amended, is a  
9 different measure than was previously attacked.

10           And I have a couple of questions that  
11 would follow from that argument, if that argument  
12 is right.

13           One, are there preconditions to Methanex  
14 under Chapter 11 bringing before an Arbitral  
15 Tribunal a measure for arbitration under Chapter  
16 11, and have they been met with respect to the  
17 current version of the California regulations which  
18 you gave us at Tab 41 in your opening? I think I  
19 will just ask you to address those questions,  
20 first.

21           MR. DUGAN: Whether all the specific

1 procedural requirements, such as the waiver and  
2 things like that have been met, no, I don't think  
3 they have been met. Obviously we have not filed a  
4 waiver on that. But, if that type of formal  
5 procedural--those procedural requirements need to  
6 be met, it seems to me that the way to do it is  
7 simple to grant an amendment to the claim. It's  
8 certainly allowed by the UNCITRAL Rules, and, in  
9 fact, as I said, the UNCITRAL Rules create a  
10 presumption that an amendment should be allowed,  
11 and there is nothing in NAFTA, as I see it, that  
12 would prevent that type of amendment.

13           But again, going back to your question,  
14 there is one point that I still to want come back  
15 to because I think it's very important. The way  
16 that the Tribunal described the impact of the CaFRB  
17 regulation in its Partial Award, we believe, is not  
18 complete, because the way the Tribunal described  
19 it, it quite clearly does ban MTBE, but as we  
20 raised in our February filing, February 2001  
21 filing, other portions of the regulation had the

1 effect of banning all competing alcohols, including  
2 methanol. And so, that prohibition was already in  
3 place.

4           Now, the measure that we were complaining  
5 of was one that banned alcohols such as methanol.  
6 The measure as it exists today has precisely the  
7 same legal operative effect. The only difference  
8 is now it names it. In our mind, that is a  
9 distinction without a difference, or a difference  
10 without a distinction.

11           If the operative legal effect of the  
12 regulations that we were complaining of in 2001 is  
13 precisely the same as is now, the California has  
14 changed its words in how it describes that  
15 operative legal effect, why is there any need for  
16 an amendment at all when we are complaining about  
17 precisely the same set of regulations that do  
18 precisely the same thing.

19           ARBITRATOR ROWLEY: But if Professor  
20 Reisman is correct, that if the regulation, the  
21 current version of the regulation is no different

1 than the original version of the regulation, and  
2 the original version of the regulation could not  
3 get you through the 1101 aperture, then why can it  
4 get you through today.

5           And I don't want to put words in your  
6 mouth, but these are the words that I--this is the  
7 distinction I understood to you make in your  
8 opening, and it was that the new version of the  
9 regulations specifically names methanol as a target  
10 of the regulation, and because it names methanol,  
11 you say that or I think you've said that we no  
12 longer had to worry about there being a showing of  
13 an intent to harm methanol because methanol was  
14 specifically named.

15           So, anyway, let me stop there. Am I right  
16 on that?

17           MR. DUGAN: You're right, that's what I  
18 said, and I still say that, and I say it for two  
19 reasons. One is because we think it is conclusive  
20 evidence of an intent to harm methanol producers;  
21 and secondly, because again, and I don't see any

1 reason why we can't put forward this in the  
2 alternative, we believe that this--California's  
3 amendment of this measure to expressly name  
4 methanol clearly satisfies the relating to/legally  
5 significant relationship test that the Tribunal  
6 posited in its Partial Award. We say it for both  
7 reasons.

8           Now, you said that the regulation is the  
9 same now as it was then. And I guess that's not  
10 precisely true. We would say the operative legal  
11 effect is the same now as it was then; i.e., that  
12 methanol was banned, but the regulation is  
13 different now because it does expressly name  
14 methanol. That's the difference.

15           ARBITRATOR ROWLEY: Yes, and I guess my  
16 point is that if there is a real difference, then  
17 is it not a different measure, and if it's a  
18 different measure, then in order to rely on it,  
19 because of it being a different measure, not for  
20 evidentiary purposes, as the President said you may  
21 be pushing on a reasonably open door for use of it

1 as evidentiary--evidence of intent, but if you're  
2 using it as a measure which, because it names  
3 methanol, we don't have to worry about intent, then  
4 you will have to get--you will have to, at the end  
5 of the day, convince us that an amendment is  
6 appropriate and that we have the power to make that  
7 amendment.

8           MR. DUGAN: Well, in terms of your power  
9 to make the amendment, I think the UNCITRAL Rules  
10 quite clearly give you that power. I don't think  
11 there is any doubt whatsoever about that. And, in  
12 fact, I don't have a copy of the UNCITRAL rule in  
13 front of me. I know Mr. Veeder does.

14           PRESIDENT VEEDER: Can I read it out  
15 because it actually highlights, I think, part of  
16 the problem we are addressing. I will read it out  
17 and then I will make the point. DUring the course  
18 of the arbitral proceedings, either party may amend  
19 or supplement his claim or defense unless the  
20 Arbitral Tribunal considers it inappropriate to  
21 allow such amendment having regard to the delay in

1 making it or prejudice to the other party or other  
2 circumstances.

3           The second sentence goes on, However, a  
4 claim may not be amended in such a manner that the  
5 amended claim falls outside the scope of the  
6 arbitration clause or separate arbitration  
7 agreement.

8           Now, the first sentence goes to  
9 discretion. The second goes to jurisdiction and  
10 power, even if we were with you as a matter of  
11 discretion.

12           And I think just to summarize, I think  
13 where we have gotten to, if this is part of your  
14 evidential case, i.e. it supplies evidence as to  
15 the intent of California relevant to the two  
16 measures you originally pleaded, as we said,  
17 subject to hearing the United States, you're  
18 pushing an open door as far as deploying this  
19 material. If you're saying that this is the same  
20 measure, but like Topsy, it grew up between 1999  
21 and 2003, but it's the same Topsy because what was

1 implicit or necessarily there but not explicit is  
2 now explicit.

3           Again, it doesn't seem to us from what  
4 you're saying that you're applying for an  
5 amendment. You're just looking at the same  
6 measure, albeit in rather more developed form.

7           But if you're going to the third stage and  
8 saying this is not Topsy, this is a new measure,  
9 this is Tom, but we haven't got Tom pleaded, the  
10 Amended Statement of Claim. We haven't got Tom  
11 identified in our Partial Award, and Tom is a new  
12 person in this arbitration, and it came effectively  
13 with your letter of the 13th of June.

14           Now, leave aside discretion, just think  
15 very hard how it is that we have power under  
16 Article XX or under our Partial Award to allow Tom  
17 to arrive, given also the terms of Chapter 11.

18           MR. DUGAN: Well, I think of the three  
19 personages that you just posited, Dick, Harry, and  
20 Tom, in terms of the first one, only because you  
21 used Tom, in terms of the first one we are

1 obviously pleading it, if nothing else, as evidence  
2 of California's intent.

3           As far as the second one, was this Harry  
4 pleaded in October of 2002. We would say yes,  
5 Harry was quite pleaded October 2002. What we said  
6 then was CaFRB's latest amendments to the CaFRB3  
7 regulations, which are to be adopted in December  
8 2002, expressly identified methanol as one of the  
9 alternatives to ethanol that are currently banned  
10 in use after December 31st, 2003.

11           PRESIDENT VEEDER: Give us the reference.

12           MR. DUGAN: Paragraph 122 of the Second  
13 Amended Statement of Claim.

14           PRESIDENT VEEDER: I will make the point,  
15 but I'm sure it's well in your mind. This is  
16 certainly a pleaded reference to the proposed  
17 regulation, which was exhibited, and we have that  
18 point. But in one view all this deploys is those  
19 proposed regulations as evidence of intent. It's  
20 not elevating it into a new separate measure, which  
21 is the subject of your complaint under 1101.

1           Now, we can go through the pleadings, and  
2 we have looked at the Amended Statement of Defense  
3 and the reply and the rejoinder, and the disputing  
4 parties' opening oral submissions, but there is an  
5 ambiguity in this Amended Statement of Claim as to  
6 whether it was deployed as evidence or, as you say,  
7 as a measure. And that's the point that troubles  
8 us.

9           MR. DUGAN: Well, again, and I understand  
10 what you're saying, but the measure that we are now  
11 complaining of is in precisely the same language as  
12 what we supplied to the Tribunal in October of  
13 2002, and in essence what he said, we were  
14 complaining about this particular regulation, and  
15 this is what it's soon going to look like. And in  
16 fact, as a factual matter, it now does look like  
17 what we told the Tribunal it would look like. It  
18 has the same operative legal effect now as it did  
19 when we actually filed this Amended Complaint,  
20 because like I said, at that time it banned  
21 methanol, although it didn't name methanol.

1           So, I guess in terms of your second  
2 category, is this the same measure that we've  
3 always been complaining of, we would say, yes, it's  
4 is the same measure we have always been complaining  
5 of. We have been complaining about a California  
6 regulation in different guises, or using different  
7 words that has the same legal effect, which is what  
8 we are worried about, which is the ban on methanol.

9           And this no more increases the ban on  
10 methanol than it was--than the previous versions  
11 did. The ban has been in place since we filed our  
12 First Amended Claim.

13           All this does is, again, no change in the  
14 operative legal effect. It uses different words,  
15 but it comes to precisely the same conclusion.

16           So, in that case we would say, to take  
17 your second category, that this is still Harry.  
18 Harry has got a different shirt on. That's all,  
19 but that different shirt makes a big difference in  
20 terms of how the Tribunal posited the relating-to  
21 test because now it expressly de jure relates to

1 methanol. So even though the operative legal  
2 effect is the same in terms for purposes of the  
3 test you posited, it's still Harry.

4           Now, to take your third category, to adopt  
5 a belts-and-suspenders approach, we do formally  
6 move to amend because we don't think that if we are  
7 allowed to amend, we don't think there is any need  
8 to resatisfy us, especially in a situation like  
9 this where the legal effect is precisely the same.  
10 I would submit to you it's within your discretion  
11 to do so, and that there is no reason why we have  
12 to meet all the various procedural requirements.

13           And finally, getting to the matter of your  
14 discretion, I mean, if this were--the way you  
15 posited the test, if this amendment were not  
16 granted, then what would be the consequence would  
17 be, I mean, if we were to lose the case and the  
18 amendment had not been granted, then we would have  
19 to refile the case and start the whole thing all  
20 over again, and we would instantly meet the legally  
21 significant test that you posited. And I submit

1 that that would be a tremendous waste of everyone's  
2 resources if we were required to do that.

3           You have the amendment before you. We  
4 identified in October of 2002 specifically what it  
5 was, that it was coming, it has now come. We see  
6 no equitable reason whatsoever why it shouldn't be  
7 before the Tribunal.

8           So, to take your three categories, we will  
9 make all three arguments, and we think under any of  
10 those three arguments we're entitled to have this  
11 placed before the Tribunal.

12           ARBITRATOR REISMAN: I would like to  
13 understand the substantive implication of the  
14 introduction of RFG3, CaRFG3, and I'm still a bit  
15 puzzled by this.

16           If RFG2, by implication, excluded any  
17 oxygenate that had not been the subject of a  
18 multimedia study, multimedia evaluation, and that  
19 was RFG2, and by implication that had to include  
20 methanol and everything else that's now listed in  
21 subsection four of RFG3, and the Tribunal did not

1 find that that established the intent to harm, and  
2 reached the threshold required under 1101, why did  
3 does the introduction of RFG3, with its explication  
4 now do that?

5           More specifically, a related question, if  
6 the Legislature says you cannot use another  
7 oxygenate until it has gone through a multimedia  
8 evaluation, and without discrimination lists all  
9 those others that have not gone through the  
10 multimedia evaluation, is that evidence of intent  
11 to harm those others?

12           MR. DUGAN: Well, it is in the context of  
13 the record here because one of the principal pieces  
14 of evidence that we say supports our case is that  
15 Governor Davis ordered the State of California to  
16 pay for the multimedia evaluation of one oxygenate,  
17 namely ethanol. None of the others. He selected  
18 out ethanol. He paid for the evaluation of that.  
19 He ordered that the steps go forward to create an  
20 in-state ethanol industry, and you know why we say  
21 that he did that.

1           So, yes, it is a conditional ban in that  
2 sense, but it is quite clear that in the totality  
3 of the facts and circumstances that it was intended  
4 by California to be in effect a permanent ban, and  
5 that's why only ethanol was selected for evaluation  
6 is because there was quite express favoritism to  
7 ethanol that was not shown to any of these other  
8 competing oxygenates.

9           But again to get back to the first part of  
10 your question, if I could, I don't think the  
11 Tribunal focused on the fact that the ban of other  
12 alcohols was also in place, and the reason why I  
13 say that is because what the Tribunal has expressed  
14 is the rationale for why, as a de jure matter, the  
15 methanol could not make a case unless it had this  
16 significant intent to harm case is because the  
17 measure that we were complaining about did not  
18 expressly name methanol. And that appears, I  
19 think, four or five times during the Partial Award.  
20 I could take you through it, but I think it's  
21 abundantly clear that, in my mind at least, that

1 was the principal reason why the Tribunal found no  
2 de jure relationship because the words weren't  
3 there.

4           Now, again, one final point. I may be  
5 beating a dead horse at this point. You asked what  
6 is the subsequent effect of this latest change for  
7 a methanol producer? There is none. It's been  
8 banned for use as an oxygenate conditionally to use  
9 the words of the United States, since for many  
10 years.

11           Subsequent--I mean, the substantive effect  
12 is really for this Tribunal because the Tribunal  
13 laid so much emphasis on the de jure aspect of the  
14 measure, that it didn't, de jure and ipso facto,  
15 ban methanol by name, and therefore this test was  
16 created. And we simply made the point, the measure  
17 as it exists now, does, indeed, do that, but in  
18 terms of its operative impact as a legal measure in  
19 California, it has no different operative legal  
20 impact.

21           ARBITRATOR REISMAN: I thank you for that

1 clarification, which is very helpful.

2 Just could you remind me, when did the  
3 multimedia study of ethanol take place?

4 MR. DUGAN: The multimedia study of the  
5 ethanol took place, it began in 1999. It was  
6 ordered, I think, in paragraph 10 or paragraph 11  
7 of Governor Davis's Executive Order of March 1999,  
8 and it took place in stages. The first stage was a  
9 lengthy study that was published in, I think, late  
10 December or early January of 1999. That study  
11 identified a number of very serious gaps with  
12 respect to the knowledge base of ethanol in  
13 groundwater in particular, and a further study took  
14 place. There was an addendum to the first study  
15 that I think was first published in February or  
16 March of 2000, and then the final portion of the  
17 study, the study of the fate and transport of  
18 ethanol in subsurface water was finally completed  
19 in October 2001.

20 PRESIDENT VEEDER: Just before we leave  
21 this topic, it would be very useful if the parties

1 together or one or the other party could prepare  
2 for us the collection of different regulations.  
3 What we have is the proposed regulations in Volume  
4 1, Tab 30 of the legal authorities to Methanex's  
5 Amended Statement of Claim. We understand that's  
6 the same document that appeared at Tab 41, at the  
7 front of Tab 41, Mr. Dugan, of your exhibits to  
8 your opening oral submissions.

9           At the same time, you handed in the final  
10 version, and some of us added it to the back of Tab  
11 41. And as you said, that's the same document as  
12 was later appended in a different format to your  
13 letter of the 13th of June.

14           MR. DUGAN: I believe that's the case. I  
15 think it will be very useful for us to get the  
16 different iterations because I'm not precisely sure  
17 of that. I know in substance for what we were  
18 talking about it was the same, but it might not be  
19 complete.

20           PRESIDENT VEEDER: What we don't have the  
21 room, although we've looked for it, is the document

1 that was before the Tribunal for the purpose of its  
2 First Partial Award.

3 MR. DUGAN: Okay. We will do that, then.  
4 Just let me warn you that the regulations  
5 themselves were very unclear, and there was a--I  
6 will dig this out for you as well. There was a  
7 clarification by the staff that they had intended  
8 to ban all alcohols except for ethanol, and then in  
9 the next iteration they did ban all alcohols except  
10 ethanol, but that was clearly their intent, but  
11 it's hard to derive from the language itself. But  
12 we will try to dig all that out and put together  
13 for you an interim set of the regulation as it  
14 developed over time.

15 (Pause.)

16 PRESIDENT VEEDER: Thank you, Mr. Dugan.

17 MR. DUGAN: Okay.

18 The second aspect of the Partial Award I  
19 would like to draw the Tribunal's attention to,  
20 it's now clear that the jurisdiction has to be  
21 based on the Findings of Fact that come out of this

1 merits hearing and not the assumed Findings of Fact  
2 that the Tribunal assumed at the time that it  
3 issued the Partial Award. And Methanex would  
4 submit that there are two significant factual  
5 changes from what was assumed by the Tribunal at  
6 the time that it issued the Partial Award.

7           In the Partial Award, repeated references  
8 to methanol as merely a feedstock for MTBE, we  
9 think that a better, more accurate characterization  
10 of the market that was there is that methanol is a  
11 feedstock for RFG, just as ethanol is a feedstock  
12 for RFG. I think Mr. Burke conceded that the  
13 market, it's a continuous supply chain, that there  
14 is no distinction in the sense of continuity  
15 between the refiners and the blenders, and so I  
16 think the whole manufacturing process has to be  
17 taken into account.

18           And when viewed that way, ethanol and  
19 methanol are both feedstocks for the manufacture of  
20 RFG.

21           And secondly, they both compete directly.

1 And I think that that's a signal fact that the  
2 Tribunal didn't assume at the time and wasn't aware  
3 of, that there was this direct competition between  
4 methanol and ethanol as oxygenates, and that the  
5 sale of one would, in some instances, result in the  
6 loss of contracts for the other, that type of  
7 direct one-to-one relationship.

8           PRESIDENT VEEDER: I think whenever you  
9 refer to testimony that we've heard, it would be  
10 very useful if you could give us the reference to  
11 the transcript.

12           MR. DUGAN: I will get back to that during  
13 my closing. It is in there. I just don't have it  
14 at my fingertips. I'm sorry.

15           So we think that once the Tribunal views  
16 the facts as we have developed them here, we think  
17 that the rationale for the specific intent to harm  
18 test may well disappear because if there is this  
19 existence of a direct competitive relationship  
20 between ethanol and methanol as oxygenates, then  
21 that in a factual way, as a factual matter, affects

1 the need for this specific intent to harm test. It  
2 creates a different set of facts that would affect  
3 whether or not or how the legally defined  
4 relationship is articulated.

5 Now, those are our two principal arguments  
6 why we don't believe the specific intent to harm  
7 test is any longer necessary in the case, that in  
8 essence it's moot. If those are two not accepted,  
9 then we filed our formal Motion to Reconsider that  
10 we filed--well, we originally raised the issue in  
11 October of 2002, and we filed our formal motion  
12 back in January, and I don't propose to go into  
13 that in any great detail unless the Tribunal has  
14 any questions, and we just propose to rest on the  
15 papers with respect to that.

16 PRESIDENT VEEDER: We have a couple of  
17 questions, and we would like to raise it first by  
18 reference to your letter of the 14th of April,  
19 2004. Do you have that letter before you? If you  
20 could turn to page four.

21 MR. DUGAN: Yes.

1           PRESIDENT VEEDER: You just referred to  
2 the formal motion to reconsider the Partial Award  
3 in October of 2002. Is that a reference to your  
4 November 2002 Amended Statement of Claim, or some  
5 other request?

6           MR. DUGAN: No, it's a reference to the  
7 November 2002 Amended Statement of Claim where we  
8 raised in substance our objection to the--what we  
9 thought as the conflict between the like  
10 circumstances test and the specific intent to harm  
11 test.

12          PRESIDENT VEEDER: But if you could just  
13 turn to your Amended Statement of Claim, where do  
14 we see a request?

15          MR. DUGAN: There is no formal request for  
16 reconsideration in the Amended Statement of Claim.  
17 We--I would characterize it most accurately as an  
18 objection to the test that the Tribunal adopted.

19          PRESIDENT VEEDER: Well, it's a criticism,  
20 but no formal request.

21          MR. DUGAN: No, there was no formal

1 request.

2           PRESIDENT VEEDER: When does the first  
3 formal request, according to you, arrive before the  
4 Tribunal, apart from the request that was made  
5 immediately after the Partial Award?

6           MR. DUGAN: Not until January,  
7 January 28th of this year.

8           PRESIDENT VEEDER: You've seen obviously  
9 the United States's objection as regards the timing  
10 of such a request. Do you have any further  
11 submissions to make?

12           MR. DUGAN: No. Beyond what we put in the  
13 correspondence, no.

14           PRESIDENT VEEDER: Okay. Thank you,  
15 Mr. Dugan.

16           MR. DUGAN: Okay.

17           Now, I think there are two other issues,  
18 two other preliminary issues I would like to go to  
19 before I start the actual closing. And those are  
20 the discovery issues. And I will touch upon them  
21 only briefly. And more as an indicator of how I

1 intend to approach it in the argument.

2           The first is our request for our third  
3 party evidence that we referred to a number of  
4 times throughout this. We made good faith requests  
5 for third party evidence, and at every juncture the  
6 U.S. blocked them, and we are now faced with a  
7 situation where there are some fairly significant  
8 evidentiary deficiencies, most obviously what would  
9 be the testimony of the Andreases and Governor  
10 Davis, for example.

11           We believe that because the United States  
12 has blocked these, that the Tribunal should draw  
13 adverse inferences against them, and I will make  
14 reference to those inferences as we go through.

15           Secondly, with respect to our request for  
16 the negotiating history of NAFTA, I just want to  
17 point out to the Tribunal that the negotiating  
18 history, at least in the form of draft texts, does  
19 exist. It has been produced by the United States  
20 in other cases. It's never been produced here. We  
21 believe that that negotiating history would quite

1 clearly shed light on issues such as how to define  
2 national treatment, how to define like  
3 circumstances, how to define fair and equitable  
4 treatment, how to define international law.

5           And as I said, the Tribunal I think is  
6 entitled to those texts. I think it puts both us  
7 and the Tribunal at a disadvantage that the United  
8 States produces them in some cases but not in  
9 others. And again, I will try to point out where I  
10 think that had they been produced, it would shed  
11 light on what the meaning of the specific treaty  
12 terms is, and ask the Tribunal to draw adverse  
13 inferences for the failure of the United States to  
14 produce any of this specific negotiating history.

15           Now, with that, I would like to turn to my  
16 actual closing.

17           PRESIDENT VEEDER: Just to make it clear,  
18 you're coming back to those two items later, aren't  
19 you?

20           MR. DUGAN: Well, I will be making  
21 reference throughout the--throughout my development

1 of the facts where I think the particular  
2 inferences should be drawn.

3 PRESIDENT VEEDER: But are you coming back  
4 to your motion for the travaux?

5 MR. DUGAN: No. I mean, I think that the  
6 time for additional evidence is past, and so we are  
7 not renewing.

8 PRESIDENT VEEDER: Well, maybe not as far  
9 as we are concerned. We would still like you to  
10 develop why you think you need the travaux for the  
11 interpretation of the particular provisions of  
12 NAFTA where you seek them given the Vienna  
13 Convention.

14 And we would also like to draw the  
15 parties' attention to a recent order made in  
16 another NAFTA proceeding by a Tribunal chaired by  
17 Professor Gaillard.

18 MR. DUGAN: Is that the Camfor proceeding?

19 PRESIDENT VEEDER: Yes.

20 MR. DUGAN: That's what I'm talking about  
21 where I believe the United States agreed to produce

1 the negotiating texts in that one.

2           PRESIDENT VEEDER: We have a copy of the  
3 order, and I hope the parties have a copy of the  
4 order also. If not, we can distribute it.

5           MR. DUGAN: No, no, I have a copy of the  
6 order.

7           PRESIDENT VEEDER: It doesn't strike us as  
8 obvious that the United States had agreed to that.

9           MR. DUGAN: Well, perhaps I'm overstating  
10 it. The United States, I think what they said in  
11 the order was that they had no objection or maybe,  
12 perhaps the other NAFTA signatories had not  
13 objected to the release of the negotiating texts.  
14 Perhaps that's all they said.

15           PRESIDENT VEEDER: I think if both sides  
16 have got copies of it, we may want to come back to  
17 it, but I think we would like to hear you a little  
18 bit more at some stage. We don't want to take your  
19 submissions out of order, Mr. Dugan, as to why you  
20 think it's important to have the travaux in this  
21 case.

1           MR. DUGAN: Let's start with the first  
2 issue in the case relating to. The Tribunal has  
3 read quite a bit of significance into the term  
4 "relating to." It may be that the travaux will  
5 indicate that the parties never read that type of  
6 significance into it. It may be that the parties  
7 would have indicated a wider scope for what the  
8 meaning of "relating to" is. It may be that there  
9 was a dispute between the United States and Canada  
10 on the one hand, and Mexico on the other, with the  
11 United States and Canada seeking to protect their  
12 investors at the time that this was negotiated and  
13 arguing for the widest possible scope for the term  
14 "relating to." And perhaps Mexico was arguing for  
15 a different scope. Perhaps there were different  
16 terms used in the drafts. Perhaps the striking of  
17 different terms and the adoption of the "relating  
18 to" language indicates that this was meant to be an  
19 expansive, an expansive legal phrase, rather than a  
20 restrictive legal phrase. We don't know obviously.  
21           PRESIDENT VEEDER: Let me put the riposte

1 to you and we'll come back to you. The time for  
2 such a request was before we made our Partial  
3 Award?

4 MR. DUGAN: Agreed.

5 PRESIDENT VEEDER: Was there such a  
6 request from Methanex for 1101?

7 MR. DUGAN: I believe there was--I'm not  
8 sure there was request for 1101, no. I know that  
9 we made a request prior to the Partial Award for  
10 certain portions of the negotiating history, but it  
11 may have been limited to 1105.

12 PRESIDENT VEEDER: I think if you have an  
13 1101 request, we would like you to identify it  
14 before the Partial Award.

15 MR. DUGAN: I don't think we do, but  
16 certainly if only in terms of the relationship to  
17 the motion for reconsideration. And I think we  
18 did--I think we did make a request for the  
19 negotiating history for 1101 at the time that we  
20 asked for clarification. And this is in August 28,  
21 2002. We said, indeed, it would be fundamentally

1 unfair to accept the United States's argument that  
2 allow 1101 requires a legally significant  
3 connection while simultaneously allowing it to  
4 withhold evidence that very likely would shed  
5 important light on the proper meaning of that term.  
6 Accordingly, Methanex respectfully renews its  
7 request for an order compelling the United States  
8 to produce any potentially relevant segments of  
9 NAFTA's negotiating history. So, that was the  
10 request that we filed in August 28th, 2002,  
11 admittedly after the Tribunal issued its order with  
12 respect to the First Partial Award.

13           And I think we have identified some of the  
14 other issues that we think would be relevant as  
15 well.

16           Fair and equitable treatment, Article 1105  
17 has been the subject of enormous debate as to its  
18 meaning, especially in light of the FTC  
19 interpretation. We think that release of the  
20 negotiating drafts could well shed light on that.  
21 If you recall, one of the issues that was raised

1 was whether the concept of international law in  
2 1105 is limited to customary international law  
3 where it includes broader forms of international  
4 law. And I think that there is evidence in the  
5 record from Mr. Aguilar that there was one draft  
6 that did include the word customary, but that that  
7 was struck. That's the type of thing, that's the  
8 type of negotiating history that I think would be  
9 relevant not just for Methanex, but to the Tribunal  
10 as well.

11           Similarly, the concept of like  
12 circumstances, how that is to be defined. There  
13 may be well be drafts that were proposed but not  
14 adopted that would shed some light as to how  
15 expansive or restrictive a legal term that is meant  
16 to be.

17           PRESIDENT VEEDER: Just to complete the  
18 procedural story, there was correspondence  
19 partially between the parties, disputing parties  
20 and the Tribunal about this request, and it was  
21 envisaged it would be dealt with at the procedural

1 hearing in March 2003, and we would like your help  
2 as to how that particular request was pursued--of  
3 that hearing.

4 MR. DUGAN: I'm not sure the negotiating  
5 history was pursued, and frankly, we never received  
6 a response from our August letter, and we never  
7 received--

8 PRESIDENT VEEDER: We need to look at the  
9 letter from the Tribunal from the 25th of  
10 September, 2002.

11 MR. DUGAN: Perhaps I have misspoken now.

12 PRESIDENT VEEDER: Well, you need not do  
13 it now, but at stage we'd like some explanation as  
14 to this request having been made, the Tribunal  
15 having responded, the procedural meeting having  
16 been held here in March 2003, why wasn't it pursued  
17 by Methanex at that time.

18 MR. DUGAN: Frankly, it wasn't pursued by  
19 Methanex at that time because we thought that the  
20 Tribunal had absolutely no interest in granting it,  
21 and we had been making a number of requests for the

1 negotiating history; a request for the 1105  
2 negotiating history I think goes back to 2001.

3           PRESIDENT VEEDER: Mr. Dugan, we can go  
4 through this, and you are entitled to criticize the  
5 Tribunal. Please don't resist if you have  
6 criticisms to make, but it ought to be fair  
7 criticism. There was a 1105 request, and we dealt  
8 with it in the Partial Award. At the time of the  
9 Partial Award, as best as we can recollect, there  
10 had been no request from Methanex for any travaux  
11 relating to 1101.

12           MR. DUGAN: And I don't dispute that.

13           PRESIDENT VEEDER: I think you agree with  
14 that?

15           MR. DUGAN: I do agree with that.

16           PRESIDENT VEEDER: After the Partial Award  
17 there was such a request, there were further  
18 intonations for travaux. And if you look through  
19 the correspondence, the Tribunal indicated that it  
20 wanted that to be discussed with the parties at a  
21 procedural meeting which eventually took place in

1 March of 2003. And before March 2003, if there is  
2 any criticism of the Tribunal, we would you like to  
3 specify precisely what it is.

4 MR. DUGAN: I don't have any precise or  
5 specific criticism the Tribunal, and as to what  
6 should have been raised in 2003, Methanex, in  
7 retrospect, probably should have raised it, but it  
8 was a matter of in litigation you pick and choose  
9 where you make your requests and where you fight  
10 your fights. And Methanex decided not to. I  
11 decided not to at that point to raise that issue,  
12 and the Tribunal didn't raise it, and the issue was  
13 put to the side. That's quite clear.

14 PRESIDENT VEEDER: For now, please don't  
15 assume the Tribunal is disinterested in your  
16 application, which it is treating as a live  
17 application. We have not determined it one way or  
18 the other, but we do need your help this afternoon  
19 as to why you still think it's relevant to have  
20 travaux on 1101, given that we made a Partial  
21 Award on the meaning of Article 1101, and just let

1 me finish. If you can go through the other  
2 requests, you're asking for the travaux in  
3 relation to 1102. You are not, I think, making any  
4 request of present in regard to 1105 or 1110, but  
5 you are in relation to Article 2101. Is that  
6 right?

7 MR. DUGAN: I think that is right.

8 PRESIDENT VEEDER: So, we are looking at  
9 1101, 1102, and 2101.

10 MR. DUGAN: Well, I mean it says that it's  
11 not exhaustive if I could amend that and ask for  
12 the history with respect to 1105, I would as well,  
13 because I think that's a very important nearby this  
14 case.

15 PRESIDENT VEEDER: And again, you've got  
16 to make out a case for it.

17 MR. DUGAN: Okay.

18 PRESIDENT VEEDER: You are going to make  
19 out a case for it.

20 MR. DUGAN: The question of what fair and  
21 equitable treatment actually means, actually

1 covers, has been, as I said, an object of quite a  
2 bit of dispute. There is dispute now, for example,  
3 about whether or not Professors Crawford's  
4 articulation of what it means in the waste  
5 management case is reflective of customary  
6 international law.

7           I think one of the things that we've  
8 argued is that 1105 is not limited to customary  
9 international law. It includes international law.  
10 That's what it says, and that's what it means, and  
11 we very much would like to see the negotiating text  
12 to see whether the word "customary" was included in  
13 one of the drafts, and then struck. We think if it  
14 was, that is persuasive evidence in that the fair  
15 and equitable treatment must be in accordance with  
16 all aspects of international law, including, for  
17 example, WTO law, and that the protections of the  
18 WTO can to some degree be imported through 1105 if  
19 1105 is meant to provide all the protections of all  
20 of international law, including treaty law, not  
21 just customary law.

1           Now, the United States has asserted that  
2 it doesn't, and they now have the FTC  
3 interpretation, which attempts to deliver the  
4 protection of that to customary international law.  
5 Methanex submits that if the phrase "customary" was  
6 strike struck from the negotiating history, then  
7 it's quite clearly the intent of the parties to  
8 include the protections of all of international  
9 law, not just customary international law. And if  
10 that's the case, then the FTC interpretation of  
11 2001 is quite clearly an amendment. It's not an  
12 interpretation, and it's an impermissible  
13 amendment. It's not an interpretation.

14           We don't know that. And all the parties  
15 have been assiduous in trying to protect themselves  
16 with respect to what the negotiating history says,  
17 and I submit that one of the reasons why they do is  
18 because they now realize that, as drafted, it  
19 provides quite broad protections for investors, and  
20 that was the intent, we submit, of the parties,  
21 specifically of Mexico--I mean, of Canada and the

1 United States, which at the time were looking for  
2 the protections that would be provided by NAFTA and  
3 looking for expansive protections just as they were  
4 in all other investment treaties that they were  
5 signing.

6           And that the arguments that are reflected  
7 in the FTC interpretation of 2001 are post hoc,  
8 after-the-fact arguments that express nothing more  
9 than buyer's remorse; that United States and Canada  
10 didn't anticipate that they would be in this room,  
11 as they are today, to the defendants in an  
12 important proceeding alleging very serious charges.  
13 They anticipated that American corporations would  
14 be in hearing rooms and the Mexican Government  
15 would be here defending these very serious charges.

16           And finding themselves in the position of  
17 defendants, they are now retroactively attempting  
18 to restrict the scope of 1105 and the scope of fair  
19 and equitable treatment. They are trying to  
20 pretend that fair and equitable do not mean fair  
21 and equitable, and we say that's nonsense. Sir

1 Robert Jennings said that was nonsense, he said  
2 that was a preposterous argument.

3 Now, could the negotiating history shed  
4 light on that? We believe that it could, but  
5 you're asking me to, in essence, speculate what's  
6 in the negotiating history. I don't know. But  
7 it's hard to believe that some concept, some  
8 expression of the potential scope of fair and  
9 equitable treatment was not raised during the  
10 course of the proceeding--during the course of the  
11 negotiation. Perhaps it wasn't. And if that's the  
12 case, then I guess we are left with trying to  
13 figure out what it means on its surface.

14 But those are the types of things that we  
15 believe could well be useful in aiding the Tribunal  
16 to understand what fair and equitable means.  
17 That's why we believe it's entirely appropriate for  
18 the Tribunal to have that negotiating history  
19 before it.

20 (Pause.)

21 ARBITRATOR REISMAN: As a matter of

1 international law's interpretive methodology, what  
2 is the relationship between text and travaux under  
3 the Vienna Convention, Articles 31 and 32?

4 MR. DUGAN: I don't have it in front of  
5 me, and I can't quite remember what the precise  
6 standard is, but I guess what I'm submitting here  
7 is that the FTC interpretation of 2001 articulates  
8 an interpretation of 1105 that I think is  
9 inconsistent with the text of 1105.

10 ARBITRATOR REISMAN: Doesn't Article  
11 31--Articles 31 and 32 deal with subsequent  
12 agreement by the parties?

13 MR. DUGAN: I think 1131 deals with it--I  
14 think it does, but the subsequent agreement is  
15 agreement as to interpretation. And our point is  
16 that if they are trying to substantively limit the  
17 scope of 1105, they can only do that by formally  
18 amending NAFTA, invoking all the known federal  
19 legislative procedures that are required before an  
20 amendment to an American treaty or a Canadian  
21 treaty takes place, and that's what they have

1 avoided. There is no doubt that they have the  
2 power to restrict the scope of 1105 if the parties  
3 agree; but if they do so, adopting all the  
4 procedures that are known to the parties to exist,  
5 i.e. in the case of NAFTA it would have to be  
6 approved by Congress. It's a trade agreement  
7 rather than a treaty.

8           So, those are the procedures that had been  
9 bypassed here, and Methanex submits that unless  
10 those procedures are adhered to, if the changes  
11 that are proposed in the FTC interpretation are, in  
12 fact, an amendment, then it's invalid. And we  
13 submit that they are. That this was not a  
14 permissible interpretation as articulated, far too  
15 narrow--it attempted to far too narrowly restrict  
16 the scope of 1105.

17           PRESIDENT VEEDER: We also need your help  
18 to understand what you intend by the phrase  
19 "travaux." We've looked to paragraph 20 of the  
20 procedural number five in the Camfor USA  
21 arbitration, and there was perhaps a rather

1 original definition of what travaux might be. But  
2 given that you're asking for travaux now, in  
3 respect to 1105 as well, we would like you to spell  
4 out what you think travaux would be relevant in  
5 these arbitration proceedings.

6 MR. DUGAN: Well, approaching it from the  
7 lex arbitrii, the U.S. definition of discovery, I  
8 think the travaux that would be relevant is the  
9 discovery that the U.S. would be liable to produce  
10 in an American court that would bear upon the  
11 meaning of these words, and in an American court  
12 that covers a lot of ground. It covers ground for  
13 everything. Obviously stuff that is legally  
14 privileged would not be covered. There is a  
15 question about certain other categories of  
16 documents, but material that is not legally  
17 privileged, such as letters back and forth between  
18 the parties, as well as negotiating texts, minutes  
19 of meetings between the parties, memoranda that are  
20 prepared for the negotiations. In the Loewen case,  
21 the United States selectively released I think one

1 or two memoranda that did include extensive  
2 discussion of the issues to be negotiated. And it  
3 indicated, and I think it's a very accurate  
4 inference to draw from the existence of those  
5 memoranda, that there was an ongoing process where  
6 the United States would develop in writing and  
7 brief the negotiators in writing as to the  
8 consequences of and as to the meaning of various  
9 negotiating positions taken by the parties. And  
10 that process, I submit, must have existed, that  
11 there must be a long document trail as to many of  
12 these provisions and as to what they say.

13           And it's that document trail that has been  
14 partially disclosed in bits and pieces that we  
15 think would aid both the Tribunal and Methanex in  
16 articulating--sorry, Methanex in articulating this  
17 case.

18           PRESIDENT VEEDER: In making this request  
19 by reference to U.S. discovery, are you limiting  
20 your request of materials that were shared between  
21 the three negotiating parties to NAFTA?

1           MR. DUGAN: It certainly encompasses all  
2 that, but to the extent that there are--I would go  
3 beyond that. To the extent there are memoranda  
4 that were used by the negotiating teams in order to  
5 understand what the issues were in the  
6 negotiations, we believe that would be relevant as  
7 well.

8           It's quite clear it would be relevant.  
9 The question, I guess, is whether it's under  
10 traditional Rule 26 procedure, that's the type of  
11 thing that normally would have to be produced.

12           PRESIDENT VEEDER: Okay.

13           MR. DUGAN: Now, with respect to the  
14 third-party discovery, I think Methanex did on a  
15 quite diligent basis raise the issue of third-party  
16 discovery at periodic integrals. I think the  
17 first--the first request was filed in October of  
18 2002, it was raised again at the March hearing, and  
19 it was raised again earlier this year. And every  
20 attempt or every time we were on the verge of  
21 taking the discovery, such as in January of 2002,

1 the U.S. objected, and we held off and waited for  
2 the Tribunal to decide. And I think the record on  
3 that is pretty clear that they used every possible  
4 avenue to block that discovery.

5           And I think the normal common law  
6 evidentiary inferences should be drawn, where a  
7 party blocks discovery, then if there is a disputed  
8 fact, and it can be shown that the testimony that's  
9 been withheld would or the testimony that has been  
10 blocked would shed light on the fact, then the  
11 adverse inference should be drawn at that point.

12           ARBITRATOR REISMAN: You're referring to  
13 the 1782?

14           MR. DUGAN: The 1782 stuff, that's  
15 correct, which as I said we first asked for, I  
16 believe, in October of 2002.

17           ARBITRATOR REISMAN: When you say block,  
18 the implication is that when a party resorts to  
19 objections available to it at law, that's blocking?

20           MR. DUGAN: Well, arguably available to it  
21 in law. There has been no showing that the

1 objections are, in fact, available to the United  
2 States. The provision calls for broad discovery  
3 powers in aid of International Tribunal which we  
4 think this quite clearly is. This fits  
5 specifically within the scope of that, and we were  
6 faced with a position where had we gone to a  
7 Federal court while the matter was still pending  
8 before the Tribunal, I think it's virtually certain  
9 the Federal court would have done nothing, pending  
10 clarification from the Tribunal as to whether or  
11 not we had the power to go before the court.

12           And so, merely by making--you're reading  
13 1782 as meaning that if you had--

14           ARBITRATOR REISMAN: If Methanex had  
15 turned to a United States court, the court would  
16 not decide until the Tribunal had endorsed your  
17 application?

18           MR. DUGAN: Until the Tribunal expressed  
19 its opinion about whether it was permissible or  
20 not, yes, as a practical matter.

21           ARBITRATOR REISMAN: Does 1782 say that?

1           MR. DUGAN: 1782 doesn't say that, but the  
2 case law expresses in many instances a preference  
3 for that, for finding out what the Tribunal  
4 actually--what the Tribunal's view is with respect  
5 to that particular type of evidence. It's not a  
6 necessity. It's not a legal necessity. There have  
7 been cases that went forward without Tribunal  
8 forward.

9           But in this case where the United States  
10 had objected to the Tribunal allowing us to go  
11 forward and where the Tribunal reserved judgment on  
12 it, I think that the United States would surely  
13 have made the same objection to the U.S. court, and  
14 the U.S. court almost certainly, in my judgment,  
15 would have said, well, let's see what the Tribunal  
16 says. If the Tribunal blocks you from going  
17 forward with this discovery, then I think the  
18 Tribunal never would have issued it.

19           So it's key what position the Tribunal  
20 takes, for all the obvious reasons. I don't think  
21 the Federal court has ever ordered discovery,

1 perhaps I'm wrong. I don't remember all the case.  
2 I don't think it's ever ordered federal discovery  
3 where an international tribunal has ordered a party  
4 not to pursue it. So, I think the attitude of a  
5 Tribunal in a 1782 proceeding is a key element, and  
6 had the Tribunal adopted the position of neutrality  
7 in January of 2003, when it first arose, then we  
8 would have had time to pursue it. As it is now, I  
9 just don't think we have time to effectively pursue  
10 that avenue.

11           And again, it's because of the U.S.  
12 objections. And we think that the U.S. should be  
13 held to account for those objections.

14           ARBITRATOR REISMAN: When you say had the  
15 Tribunal adopted position of impartiality or  
16 neutrality. Can you explain that.

17           MR. DUGAN: Sure. In January 2002, we  
18 raise the issue in October--we raised it again in  
19 October of 2002. We raised it again, I believe, in  
20 January 2003, and as I recall the documentary  
21 record, and I haven't reviewed it for a while, so

1 I'm not entirely clear, I may be off in some of the  
2 details, the Tribunal at first adopted a position  
3 that it was appropriate for Methanex to go out and  
4 obtain this evidence if it wanted to. The United  
5 States then objected and said, no, that wasn't  
6 appropriate until there was an affirmative order  
7 from the Tribunal.

8           The Tribunal then sent out some letters,  
9 which we took as meaning that it wanted to review  
10 this issue at the March 31st hearing, the issue  
11 being whether Methanex could go off on its own  
12 without the endorsement of the Tribunal in response  
13 to the U.S. objection.

14           The issue was discussed at the March 31st  
15 hearing in considerable detail. At that point, the  
16 Tribunal issued an order, an oral order, to the  
17 effect that it wasn't minded at that point to, and  
18 I can't quite remember how it's phrased, to either  
19 allow or order the discovery requested.

20           PRESIDENT VEEDER: No, no, no. You may  
21 want to review this very carefully, and please

1 don't hesitate to express any criticism that you  
2 have in mind, but the Tribunal was never minded to  
3 require Methanex not to apply to a state court  
4 under 1782, so that was, I hope, always made clear.  
5 What was not made clear was whether the Tribunal  
6 should bless such an application; i.e., by granting  
7 you the approval of the Tribunal for such a  
8 request.

9           The other matter that we're going to  
10 invite to you raise, today if you can, is the way  
11 that 1782 and the Tribunal's rule under 1782, which  
12 is not explicit, ties in in this case with the IBA  
13 Rules, Article 4(10) and Article 3(8), which at one  
14 stage was an argument being raised by the United  
15 States as a qualification on your application in  
16 regard to 1782.

17           MR. DUGAN: Well, I guess taking the first  
18 issue, with all due respect, it certainly was not  
19 clear to Methanex that Methanex was free at that  
20 point to go forward with its own application. And  
21 in that respect, the Tribunal indicated that it

1 would be issuing a letter or a decision shortly,  
2 and a decision was never issued, and I think had  
3 the decision been issued, perhaps at that point it  
4 would have been clear. But not having any  
5 affirmative decision or any decision from the  
6 Tribunal, we continued in the posture that we were  
7 in, which is consistent with our understanding that  
8 we were not entitled to go forward unless the  
9 Tribunal had said either it's blessed or you may do  
10 what you want. That was the position--

11           PRESIDENT VEEDER: We have to look back at  
12 the transcript, but during the March 2003 hearing,  
13 as I recall, it was your argument that you didn't  
14 need the positive blessing of the Tribunal to make  
15 an application under 1782. That was the argument  
16 of the United States.

17           MR. DUGAN: Correct, but that we wanted  
18 the blessing of the Tribunal.

19           PRESIDENT VEEDER: You wanted the  
20 blessing, but you didn't need it.

21           MR. DUGAN: That's correct.

1           And it was our understanding that the  
2 Tribunal--the objection of the United States was  
3 that we couldn't do it unless we had the blessing  
4 of the United States--blessing of the Tribunal, and  
5 it was that issue that was never decided. There  
6 was a clear objection from the United States.  
7 There was no decision, and the effect was,  
8 certainly in our minds, to prevent us from  
9 obtaining 1782 evidence.

10           Now, in terms of, you know--

11           ARBITRATOR REISMAN: As I understood the  
12 sequence of events, the position of the Tribunal  
13 was on the record that Methanex could proceed, that  
14 it was not minded at that time to issue an  
15 endorsement, that as to the question of whether it  
16 would issue an endorsement it would take that under  
17 advisement, but the general license of Methanex to  
18 proceed under 1782 was never in doubt.

19           MR. DUGAN: With all due respect, I don't  
20 believe that there is an toward that effect. And  
21 again, that would have required a ruling on the

1 objection of the United States that we lacked that  
2 power, and there was no ruling on the objection of  
3 the United States that we lacked the power to go  
4 forward independently.

5           PRESIDENT VEEDER: Mr. Dugan, do you  
6 remember the debate? I'm sorry to get back to the  
7 March hearing. We indicated that was something  
8 that this Tribunal could not decide. It had to be  
9 for a court to decide whether or not the Tribunal's  
10 blessing was required or not in the exercise of  
11 that court's jurisdiction.

12           MR. DUGAN: I will go back and read the  
13 transcript.

14           PRESIDENT VEEDER: I will give you one  
15 reference which I do recall, which is that--this is  
16 the transcript for the 31st of March, and I'm  
17 reading from page 108, 109, what was said on behalf  
18 of Methanex was this:

19                       We have always taken the position  
20                       with the Tribunal that we didn't believe  
21                       that the Tribunal's blessing was necessary

1           in order to invoke 1782, and then you  
2           referred to your October letter. And you  
3           concluded, In the best of all possible  
4           worlds, we would prefer a Tribunal order,  
5           but if the Tribunal, for whatever reason,  
6           is unwilling to issue it, we believe that  
7           under the statute we are entitled to go to  
8           the District Court as an interested party  
9           and seek to convince the District Court to  
10          grant us this additional evidence. In  
11          other words, while we would welcome a  
12          Tribunal order, we don't believe it is  
13          necessary for us to succeed at the  
14          District Court level, and I don't believe  
15          that position has changed.

16          Now, clearly, you wanted our pressing  
17          because you thought it would help, but our  
18          recollection is that you didn't say you needed it  
19          to make the application.

20               MR. DUGAN: But we also wanted a ruling on  
21          the U.S. objection, which is what we were expecting

1 would happen, and the U.S. had quite clearly made a  
2 ruling--made an objection--and what we were afraid  
3 of, without a ruling on the U.S. objection as to  
4 whether we had that power, if we went into a  
5 Federal court, the United States would make the  
6 same objection that this is pending before the  
7 Tribunal. It would be premature for this court to  
8 take any position with respect to a 1782 request  
9 until the Tribunal has issued a decision on the  
10 U.S. objection, which it indicated it would be  
11 issuing soon. And so, that's why we didn't do it.

12 PRESIDENT VEEDER: Thank you, Mr. Dugan.

13 MR. DUGAN: Would this be an appropriate  
14 time to take a break and I could come back and  
15 begin the closing.

16 PRESIDENT VEEDER: I'm sorry if we have  
17 taken you out of turn. I think we should take a  
18 break. We have a shorthand writer who has taken  
19 down a lot of words this afternoon. Let's take a  
20 10-minute break.

21 (Brief recess.)

1           PRESIDENT VEEDER: Let's resume.

2           Mr. Dugan, I'm conscious that we have been  
3 interrupting you, and we apologize for that, but  
4 it's certainly been very helpful to have this  
5 exchange with you, and we thank you for answering  
6 our questions, but we don't want to remove your  
7 allocation of time because of what we call injury  
8 time from the Tribunal. So, we can go beyond 5:30  
9 this afternoon. Please don't feel that you have to  
10 speak any faster or truncate any of your  
11 submissions.

12           MR. DUGAN: Thank you. I appreciate that.

13           All right. To begin with, proceeding on  
14 the assumption that Methanex does have to meet the  
15 standard set forth in the Partial Award, a specific  
16 intent to harm, later in my presentation I will go  
17 over what evidence we think clearly supports that  
18 inference. So, it will come at a different portion  
19 in the presentation today.

20           Now, the first issue I would like to turn  
21 to is 1102, but before we actually turn to 1102, I

1 think it's necessary to deal with the governing law  
2 issue and what law is to be relied upon by the  
3 Tribunal in resolving this.

4           Now, obviously, Article 1131, which we  
5 will put up as a slide, states quite clearly what  
6 the Tribunal is to rely upon. A Tribunal  
7 established under this section shall decide the  
8 issues in despite in accordance with this agreement  
9 and applicable rules of international law.

10           Now, international law usually includes  
11 under Article 38 of the ICJ, jurisprudence,  
12 international jurisprudence.

13           The U.S. argue that is WTO law and GATT  
14 law has no on place in this proceeding. So, in  
15 essence, what they want 1131 to say is this: A  
16 Tribunal established under this section shall  
17 decide the rules, the issues in despite in  
18 accordance with this agreement, and applicable  
19 rules of international law, except for WTO, GATT  
20 law, and national treatment because they decided  
21 that they really don't much like that law, and I

1 think to phrase it that way to expresses precisely  
2 what's going on here. The United States is trying  
3 to pick and choose which issues, which areas of  
4 international law apply, and they can't do that.  
5 Under 1131 the Tribunal is required to take into  
6 account all of international law, not just  
7 customary international law, but all of  
8 international law. And that's the standard.

9           So, the U.S. statement that WTO law has no  
10 place in this dispute is simply wrong as a matter  
11 of the governing law.

12           Now, I'd also point out that in cases such  
13 as Pope and Talbot, they rely on WTO law. So,  
14 there is traditional of NAFTA Tribunals relying on  
15 WTO law, and we think it's perfectly appropriate  
16 for the Tribunal to do so here.

17           Now, this also points out two other  
18 issues. This is a place where negotiating history,  
19 I think, could be very useful, to see exactly what  
20 law does apply. We don't have that here. The  
21 United States is arguing for interpretation of 1131

1 that can't be supported by the text of the  
2 provision. And if that's the case, it seems to me  
3 incumbent upon the United States to produce any  
4 relevant negotiating history.

5           The second point I would like to make is I  
6 don't think that the--even if there had been, for  
7 example, an STC interpretation saying that WTO law  
8 has no role in NAFTA dispute, that the parties have  
9 the power to do that. This is a good example of  
10 what would be an impermissible amendment.

11           The parties, by agreement, three parties  
12 who are defendants in numerous suits by agreement  
13 cannot issue an interpretation that reads a  
14 specific area of law out of the Treaty. They can  
15 only do that by formally amending the Treaty.  
16 That's too distinct and too important a deletion  
17 from the Treaty to be anything other than an  
18 amendment.

19           Now, the first point I would like to make  
20 is 1102, and what it is that 1102 prohibits. The  
21 U.S. argues that 1102 prohibits discrimination

1 against foreign investments because they're  
2 foreign. Now, that's surely true. No one can  
3 dispute or quibble with that interpretation, but  
4 1102 prohibits something else as well. It  
5 prohibits discrimination that favors a domestic  
6 industry. And again, what's the legal basis for  
7 this? The legal basis for this is the express  
8 language of 1102: A foreign investment is entitled  
9 to the most favorable treatment as a domestic  
10 industry receives. If the domestic industry is  
11 favored, then the foreign investor is equally  
12 entitled to that favored status.

13           So it's not simply discrimination against  
14 an investment because it's foreign owned, although  
15 we think that took place here. That's not all that  
16 1102 prohibits. It prohibits favoritism. It  
17 prohibits economic protectionism. It prohibits  
18 precisely the type of behavior that we contend the  
19 United States and California engaged in here.

20           And once again, the fact that California  
21 may have discriminated against U.S. methanol

1 producers while it was favoring U.S. ethanol  
2 producers is irrelevant. And I think the case that  
3 best serves this point is the European Commission  
4 versus Denmark where they were trying to determine  
5 whether there was discriminatory intent in a Danish  
6 tax provision.

7           Now, a statement there said, viewed by  
8 itself the tax system introduced by the Danish  
9 legislation contains incontestable discriminatory  
10 or protective characteristics. Although it does  
11 not establish any formal distinction, according to  
12 origin of the products, it is has been adjusted so  
13 the bulk of the domestic production of spirits  
14 comes within the most favorable tax category,  
15 whereas all imported products come within the most  
16 heavily tax category. These characteristics of the  
17 system are not obliterated by the fact that a very  
18 small fraction of imported spirits benefits from  
19 the most favorable rate of tax, whereas conversely,  
20 a certain proportion of domestic production comes  
21 within the same tax category as imported spirits.

1           It therefore appears that the tax system  
2 is devised so that it largely benefits a typical  
3 domestic product and handicaps imported spirits to  
4 the same extent.

5           Now here, the California regulatory  
6 scheme, the ban on MTBE, and the ban on all the  
7 competing oxygenates, including methanol, largely  
8 benefits the U.S. ethanol industry which, as we  
9 have seen, produces 93 percent of the ethanol  
10 consumed in the United States. And it handicaps  
11 foreign methanol and MTBE to the same extent.

12           Now, one of the things that came out in  
13 the hearing was testimony by Mr. Burke, I believe,  
14 who testified at page 1425. The question was:

15                       So, if 47 percent of the methanol  
16                       operating capacity is domestically owned,  
17                       that would mean that the majority or  
18                       53 percent is foreign owned; is that  
19                       correct?

20                       That's correct.

21           So, we are dealing here with an industry

1 that is majority foreign owned, and that's in  
2 considerable contrast to the United States's  
3 ethanol industry, and that's an important fact for  
4 the Tribunal to consider.

5           Now, if 1102 prohibits favoritism to a  
6 domestic industry, then one of the key issues here  
7 obviously is whether California and former Governor  
8 Davis intended to, and did, in fact, favor the U.S.  
9 ethanol industry. So what I would like cover is  
10 the evidence of an intent to favor, and  
11 specifically the evidence that there was some type  
12 of implicit arrangement between Davis and the U.S.  
13 ethanol industry.

14           Now, as a preliminary point, we think that  
15 the evidence that was adduced during the hearing  
16 also shows fairly clearly that MTBE was singled out  
17 in contrast, for example, to benzene.

18           Again, there was no doubt there was  
19 testimony to this effect. Benzene is a known  
20 carcinogen, and it's one of the worst components of  
21 gasoline.

1           Now, Dr. Happel, in response to a question  
2 about the NRDC listing of the most prevalent  
3 contaminants in California's water, the one that  
4 lists benzene but does not list MTBE, said she had  
5 done her own analysis, and she had come to a  
6 different conclusion. And what she said at 1208 of  
7 her testimony, and this is lines 11 through 16:

8           Use of the primary MCL value of 13  
9 parts per billion for MTBE would show that  
10 the percentage of public drinking water  
11 wells with detections of MTBE at or above  
12 the primary MCL is nearly equivalent to  
13 benzene. By the use of this primary MCL,  
14 MTBE would rank 14th in this analysis.

15          Well, what's significant about that is  
16 that even their own expert concedes that benzene is  
17 a worse problem than MTBE. Now, if that's the  
18 case, what's California doing about benzene?  
19 Nothing. They may be reducing it, but they're  
20 certainly not eliminating it. They're not taking  
21 benzene anywhere near as seriously as they took

1 MTBE. And that's an important fact to consider  
2 because benzene is universally acknowledged to be  
3 more dangerous and damaging than MTBE is, because  
4 it is a carcinogen, a known carcinogen.

5 Now, there is no doubt that they could  
6 have acted, that California could have acted. It  
7 could have taken steps with respect to benzene.  
8 Burke testified again at page 1475, lines 6 through  
9 13:

10 But you would agree that if the EPA  
11 can ask refiners to remove sulphur, it can  
12 ask refiners to remove benzene; is that  
13 correct?

14 Well, the EPA has asked refiners to  
15 reduce benzene content, and they could ask  
16 them to remove it too, couldn't they?

17 I suppose they could.

18 So, taking action against benzene was  
19 perfectly feasible for California to do. It  
20 didn't.

21 Now, he took the position that it was

1 prohibitively expensive. But I would like to draw  
2 your attention to a chart that was shown to  
3 Mr. Burke during his cross-examination. This chart  
4 shows that the cost of taking 70 percent of the  
5 benzene out of gasoline, last number down there,  
6 was .67 cents per gallon, and right above that it  
7 shows that the cost of using ethanol in California  
8 was 3.9 cents a gallon.

9           So, it was approximately six times more  
10 expensive to use ethanol than it would have been to  
11 reduce benzene, and yet California showed  
12 absolutely no interest in meeting the benzene--in  
13 dealing with the benzene problem.

14           MR. LEGUM: Mr. President, we would like  
15 to note our objection to this use of this document.  
16 It was offered for addressing the credibility of  
17 Mr. Burke's testimony. This is now being offered  
18 as primary evidence that if it was to be relied on,  
19 should have been submitted with Methanex's reply or  
20 before.

21           PRESIDENT VEEDER: I think we're going to

1 need to look at the passage of Mr. Burke's evidence  
2 because we do recollect the challenge made to the  
3 United States and the way in which this document  
4 was allowed to be put to Mr. Burke.

5 MR. DUGAN: I don't think we have the  
6 actual passage. I don't know the actual passage  
7 where he was.

8 I will withdraw the document.

9 ARBITRATOR REISMAN: Could I get a  
10 clarification, please. Dr. Happel was testifying  
11 about groundwater and, as I recall, the issue there  
12 was whether or not MTBE undergoes ambient and  
13 transient bioremediation as does benzene; that if  
14 there is a spill, the benzene undergoes an  
15 intrinsic bioremediation, and that MTBE did not.

16 Wasn't that the issue of benzene that the  
17 context in which she made that point?

18 MR. DUGAN: I don't believe it was. I  
19 believe what she was responding to was the  
20 criticism that the MTBE was not as serious a  
21 contaminant as benzene was, and she took

1 dispute--she disputed, she took issue with the NRDC  
2 chart and said that, no, in fact, under her  
3 analysis it was almost as serious as benzene and  
4 that it would have ranked in the chart of the top  
5 24 contaminants.

6           And the question of biodegradation I think  
7 is a different question. It's a precedent  
8 question, and the comparative rates of  
9 biodegradation would affect the contamination of  
10 drinking water. But I think that's what she was  
11 talking about, was where it ranked on the list of  
12 list of comparative contaminants of drinking water.

13           So, I offer that for the purpose of just  
14 showing that even their expert recognized that the  
15 threat actually posed to drinking water which,  
16 remember is what the NRDC chart was intended to  
17 show, was still, even under their own expert's  
18 calculation, showed that benzene was worse as a  
19 contaminant in terms of its prevalence of  
20 California's drinking water than MTBE is.

21           Now, California has not acted anywhere

1 near as aggressively against benzene as it did  
2 against MTBE, and we ask the question why.

3 ARBITRATOR ROWLEY: Mr. Dugan, is there  
4 evidence before us that benzene was perceived to be  
5 a problem in California to the same extent, at the  
6 same time that MTBE was perceived to be a problem?

7 MR. DUGAN: No. There isn't evidence, and  
8 there is a reason for that, and that's the reason  
9 that we tried to set out, which is that the relying  
10 upon the two news stories that we put into the  
11 record, that ADM went about hiring people to stir  
12 up, to whip up hysteria about MTBE. Oxy Busters,  
13 that whole front organization that was described in  
14 the two articles, I think, and Methanex thinks,  
15 explains why MTBE was perceived to be a problem,  
16 and benzene was not. It was because the ethanol  
17 industry stood to benefit if it could eliminate  
18 MTBE as a competitor, and there was no comparable  
19 U.S. industry that was interested in getting rid of  
20 benzene.

21 PRESIDENT VEEDER: Just for the record, in

1 case we come back to it, Mr. Dugan, I think the  
2 reference to our ruling in relation to the document  
3 you've just withdrawn is at page 1466 of day six.

4 MR. DUGAN: I'm sorry, I wasn't aware of  
5 the ruling, so I--

6 PRESIDENT VEEDER: It was expressly put in  
7 by Ms. Callaway in her words--well, the comment was  
8 made, Ms. Callaway, is this document in the record,  
9 for the United States?

10 MS. CALLAWAY: No, it is not. It is  
11 used for credibility and goes directly to  
12 the conclusion regarding the cost of  
13 reducing benzene content. It was put in  
14 on the basis of credibility only and not  
15 as evidence of its contents.

16 MR. DUGAN: Well, I remember Mr. Burke's  
17 testimony, his witness statement was that the cost  
18 was prohibitively expensive. I think that to a  
19 degree this undercuts that. So, if it's taken in  
20 for the purposes of challenging Mr. Burke's  
21 credibility, it seems to me it's properly before

1 the Tribunal.

2           PRESIDENT VEEDER: As an attack on his  
3 credibility, but not as evidence on its own, that's  
4 the point. But maybe you want to think about it a  
5 little bit further.

6           MR. DUGAN: I understand. I will withdraw  
7 the document, that's fine.

8           But our point, even without that document  
9 is that they were, at worst, comparable problems  
10 and yet California took no steps. It only singled  
11 out MTBE, and there is no--there is no asserted  
12 health or environmental reason why it would go  
13 after one and not the other, and Methanex submits  
14 that the reason is because of the favoritism that  
15 was shown to the U.S. ethanol industry.

16           Now, turning to what is really in many  
17 ways the central issue of the case, Professor, you  
18 focussed during my opening on a critical aspect.  
19 You asked me does Methanex contend that wherever a  
20 political contribution is followed by governmental  
21 acts favoring the contribution, is it invariably

1 corrupt, and I said no, of course not. It's a  
2 question of the particular facts and circumstances  
3 that surround the case. And that is the--that's  
4 the situation here.

5           I think you have to start with the  
6 proposition that the U.S. now finally concedes, or  
7 it was forced into conceding because of the  
8 language in the Supreme Court decision, and the  
9 language of the Solicitor General and the words of  
10 Senators like Senator Rudman and Senator McCain  
11 that there do exist situations, instances in the  
12 United States of corruption, and that's the word  
13 the Supreme Court used, that are not criminal acts,  
14 there is no quid pro quo, but there are nonetheless  
15 corruption where contributions are given and favors  
16 are granted in return.

17           To use again Senator Rudman's words, money  
18 affects outcomes, and it was that type of  
19 corruption that the Supreme Court approved--it was  
20 that context in which the Supreme Court approved  
21 the McCain-Feingold campaign reform bill.

1           Now, if you start with the proposition  
2 that these types of instances do, in fact, exist,  
3 Methanex submits that look at the evidence in this  
4 case, and determine what conclusion you can arrive  
5 at. I think the only way a decision maker can  
6 determine whether this type of corruption exists in  
7 a particular case is to fairly weigh the evidence,  
8 all the evidence, all the facts and circumstances.

9           So, let's review the evidence here. First  
10 of all, let's start with the industry. The  
11 industry we are talking about is the U.S. ethanol  
12 industry which the United States, by its own  
13 admission, and we put this slide up before, we  
14 won't put it up again, the General Accounting  
15 Office, the investigating arm of the United States  
16 Congress, said that the industry exists only  
17 because of political decisions. Without  
18 congressional approval of the tax credit,  
19 commercial ethanol production would cease.

20           So, this is an industry that owes its very  
21 existence to political favoritism. It was created

1 and it survives only because of continuing  
2 governmental favoritism. It was created and it  
3 survives only because of continuing governmental  
4 favoritism. It's not like the ethanol industry.  
5 It's not like the gasoline industry. It's not like  
6 the automobile industry. It's not like the corn  
7 industry. Those industries would exist without the  
8 Federal tax--regardless of Federal action.

9 PRESIDENT VEEDER: Just a correction to  
10 help us later. You said it's not like the ethanol  
11 industry. You meant like the methanol industry.

12 MR. DUGAN: That's correct. Thank you  
13 very much. It's not like the methanol industry.

14 All those industries exist independent of  
15 a Federal grant of tax relief. The ethanol, the  
16 commercial ethanol industry does not. It exists  
17 only because, as Senator McCain put it, ADM has  
18 used--has traded its political contributions for  
19 the tax subsidy.

20 Second, second point to take into account,  
21 who is making the contributions here? It's ADM.

1 ADM and Vind, but certainly ADM with a company with  
2 an undisputed record of influence seeking and  
3 corrupt, indeed, illegal acts, all of which is in  
4 the record, and again, to use Senator McCain's  
5 words, ADM traded political contributions for the  
6 Federal tax subsidy.

7           And there is no doubt that that's what  
8 Vind and ADM looked for when they made  
9 contributions. Let's go, if we could, to  
10 Mr. Vind's own witness statement. He said, From  
11 time to time ADM and my companies jointly sponsored  
12 legislation encouraging increased use of ethanol  
13 and as part of this effort we jointly and  
14 independently supported various legislators and  
15 members of Congress whom we felt might support the  
16 expanded use of ethanol.

17           ARBITRATOR ROWLEY: Is this Vind at page  
18 988?

19           MR. DUGAN: No, no, I'm sorry. This is  
20 Vind's witness statement, his written sworn  
21 statement that he put in prior to his

1 cross-examination testimony.

2 ARBITRATOR ROWLEY: Is it part of your  
3 package?

4 MR. DUGAN: It should be part of the  
5 package of the--

6 ARBITRATOR ROWLEY: If you can refer us to  
7 tab numbers when you are--

8 MR. DUGAN: Certainly.

9 ARBITRATOR ROWLEY: That would be helpful.  
10 Thank you.

11 MR. DUGAN: It's the last two pages of  
12 Tab 5.

13 PRESIDENT VEEDER: Which is what paragraph  
14 number?

15 MR. DUGAN: It's paragraph number four.

16 So, in Vind's own express words, what he  
17 and ADM were looking for was politicians who would  
18 support the expanded use of ethanol. That's what  
19 they wanted. That's why they made political  
20 contributions. And his testimony confirms that.

21 And this is from page--I believe it's page

1 975 of Mr. Vind's testimony, and it states, line  
2 six:

3           You were looking for legislators who  
4           would support the expanded use of ethanol?

5           That is correct.

6           And it was to those legislators you  
7           directed your contributions; correct?

8           That's correct.

9           So it's clear what they were looking for.  
10          Someone who would expand the use of ethanol.

11          He goes on, page 976:

12                 THE WITNESS: I would raise money for  
13                 legislators in California at the Federal  
14                 level who supported the use of ethanol as  
15                 a renewable fuel and expanded use of  
16                 ethanol and expanded production of  
17                 ethanol, that is correct.

18                 Now, if you had a legislator either  
19                 at the state level and Federal level and  
20                 you gave them money but they refused to  
21                 support the expanded use of ethanol, would

1           you continue to raise money for them?

2           Probably not.

3           Again, I think Mr. Vind is making it as  
4 clear as he possibly can, not as he possibly can.  
5 He's making it quite clear that the intent is to  
6 give contributions in exchange for politicians who  
7 would give him expanded use of ethanol. And it was  
8 exactly in terms of what he was looking for with  
9 respect to then-Senator--Representative and Senator  
10 Torricelli. Page 988 of his testimony, line 15:

11           You were looking for help from

12           Mr. Torricelli on your El Salvador?

13           I was looking for help from

14           Mr. Torricelli on my problem in El

15           Salvador, that is correct.

16           And you were also looking for help

17           from Mr. Torricelli on the ethanol fuel

18           tax excise credit; correct?

19           Yes, I believe so.

20           So, Mr. Vind frankly admits what he's

21 looking for. He's looking for legislators who will

1 favor his interests, and that's why he makes  
2 contributions.

3 PRESIDENT VEEDER: Just to make it  
4 absolutely clear, somebody who makes a contribution  
5 to a politician looking for a quid pro quo,  
6 Mr. Dugan, by itself, that is not a criminal  
7 offense.

8 MR. DUGAN: No, that is not a criminal  
9 offense unless there is a quid pro quo. As I  
10 understand the criminal aspects of the law, unless  
11 there is an express quid pro quo.

12 PRESIDENT VEEDER: So if the politician is  
13 expressly or by some understanding agreeing to a  
14 quid pro quo that makes it an illegal act?

15 MR. DUGAN: By expressly doing so, that  
16 would make it an illegal act, unless clear about  
17 whether it would be illegal or implicit.

18 Remember, the Supreme Court went to great  
19 lengths to distinguish that type of quid pro quo  
20 illegality and other types of corrupt implicit  
21 agreements where, again, to use Senator Rudman's

1 words, money affects outcomes, and it was that they  
2 were concerned with in upholding the  
3 constitutionality of McCain-Feingold. But for  
4 purposes of what I'm trying get across is, that  
5 type of not necessarily illegal corruption does  
6 exist. And it's corrupt.

7           PRESIDENT VEEDER: But it's not corrupt in  
8 seeking to give money to a politician to do  
9 something, and when he doesn't do it, to cease  
10 giving him money to it him. When I say him, I mean  
11 full campaign contributions, irrespective of the  
12 donor?

13           MR. DUGAN: Well, I mean, I think--without  
14 an express agreement, the money affects the  
15 outcomes, yes, I think that is corrupt, and I think  
16 that is exactly what the Supreme Court said. And I  
17 think that's exactly what the Solicitor General  
18 said.

19           And the fact that you can't prosecute it  
20 criminally because you don't have sufficient  
21 evidence of a quid pro quo connection does not mean

1 that it's corrupt. When money affects outcomes,  
2 when a legislator favors an interest because he's  
3 received a large political contribution--

4 PRESIDENT VEEDER: Forgive me, you are  
5 moving away from the donor to the donee. Mr. Vind,  
6 of this world, who gives political contribution  
7 almost always is intending to affect the result of  
8 that politician's future acts?

9 MR. DUGAN: Right. And if the  
10 politician--

11 PRESIDENT VEEDER: That's the point. At  
12 that point, there is nothing morally or legally  
13 criminal or corrupt, is there, as regard the donor?

14 MR. DUGAN: There is certainly nothing  
15 criminal about it, but I would submit that's not  
16 necessarily true, and I think ADM is a good  
17 example. That makes contributions to politics of  
18 all parties because it expects that its money would  
19 buy it favorable outcomes.

20 PRESIDENT VEEDER: That point. Both  
21 parties, the point made by the Solicitor General is

1 you're buying access.

2 MR. DUGAN: And not just access. To use  
3 the words of Senator Rudman, money affects outcome.  
4 It's not just access. It's attempt to influence  
5 the outcome of policymaking decisions through the  
6 use of money, and I think again the Supreme Court  
7 and the Solicitor General, Senator McCain, Senator  
8 Rudman quite clearly said that that's what happens.  
9 And they think it's corrupt, and they think it  
10 should be stopped. And one of the questions for  
11 this Tribunal to decide is: Is that unfair and  
12 inequitable? And we submit that it is. We think  
13 it's arbitrary and its unjust, and if it results in  
14 favoritism for a local industry, then it's  
15 prohibited by NAFTA as an improper investment  
16 practice.

17 ARBITRATOR ROWLEY: Mr. Dugan, as I  
18 understand your case at this stage, it is that  
19 California, as led by Governor Davis, did not act  
20 to cure a perceived problem because of the problem,  
21 but it acted on the basis of Governor Davis'

1 corruption, and the corruption being that he  
2 directed to the extent that he was able, California  
3 to act with the purpose of benefiting ethanol and  
4 with the purpose of disadvantaging foreign methanol  
5 producers.

6 MR. DUGAN: That's correct.

7 And the key to it, we believe, are the  
8 decisions that we think show quite clearly that he  
9 acted to benefit the U.S. ethanol industry.

10 Now, the third point is, who is receiving  
11 the contributions here? It was Gray Davis,  
12 Governor Gray Davis.

13 Now, many people in California have  
14 labeled him the "coin-operated Governor." That's  
15 not Methanex's label. That's California's label.  
16 And Governor Davis was the object of a successful  
17 recall campaign that was one of the most  
18 humiliating recalls in American political history,  
19 and there is evidence in the record that we have  
20 supported that one of the key factors in that  
21 recall was that perception of corruption, The

1 Sacramento Bee newspaper. Is it simply a  
2 coincidence? Many people in California did not  
3 believe it was simply a coincidence. They thought  
4 that it can certainly be inferred from what  
5 happened that they thought that there was too much  
6 money affecting outcomes. Again, to use Senator  
7 Rudman's words.

8           So, Gray Davis is not Mother Teresa. He's  
9 in a different category.

10           Fourth, at the time of the secret meeting,  
11 ADM had not yet decided to support Gray Davis.  
12 They hadn't made up their mind whether to support  
13 him, and we get that from Mr. Listenberger's  
14 witness statement. This is paragraph two of  
15 Mr. Listenberger's written witness statement. It  
16 was my understanding that the dinner was arranged  
17 in order for me and others to meet Mr. Davis,  
18 discuss his candidacy, and assess whether to  
19 support his campaign.

20           PRESIDENT VEEDER: He had already given  
21 him three campaign contributions?

1           MR. DUGAN: Yes, they'd given him minor  
2 contributions, but in California contributions of  
3 \$15,000 are not big money, and I think that shows  
4 in terms of what they gave him after the meeting,  
5 where they gave him at least another \$150,000 after  
6 the meeting. And they were known for being very  
7 generous supporters for those whom they supported,  
8 and Davis knew that.

9           PRESIDENT VEEDER: Do we know, does the  
10 record show if they supported his opponents?

11          MR. DUGAN: I don't know whether the  
12 record shows that or not. I just don't know.

13          But in any case, the purpose of the  
14 meeting was for ADM to decide whether or not to  
15 support Gray Davis. As we now know, they jumped in  
16 and they supported him very, very heavily, very,  
17 very generously.

18          Now, fifth, the meeting was secret, and  
19 the United States placed up before you and will  
20 place it before you again the campaign reporting  
21 form in which ADM reported the use of an airplane,

1 and as I think you pointed out, Mr. Veeder, this  
2 does not disclose where the plane was flying to or  
3 from. It simply says use of an airplane. It  
4 doesn't in any way disclose the existence of the  
5 secret meeting.

6 In addition, we have been unable to find  
7 any evidence that ADM ever disclosed the value of  
8 the dinner itself. In comparison to the next page  
9 where you see that Mr. Jack Cox reported dinner  
10 costs. We have never seen any dinner costs  
11 reported by ADM with respect to the dinner that  
12 they hosted for Gray Davis, which was quite clearly  
13 a fundraising dinner.

14 So, we think the evidence is very  
15 compelling that they intended to keep this secret.

16 PRESIDENT VEEDER: Is there not a minimum  
17 cutoff below which you don't have to declare?

18 MR. DUGAN: That, I don't know, and  
19 perhaps that's the reason--I don't know. The  
20 cut-off here was \$480, so I don't know. Perhaps  
21 that is the reason. Above that it's \$426.

1           Now, sixth, everyone agrees that ethanol  
2 was discussed at the meeting in Illinois.  
3 Listenberger agreed to it in his witness statement  
4 in paragraph five, in his transcript at page 775,  
5 lines two to four. Vind agreed to it in his  
6 transcript at 964 and 966.

7           So, there is no doubt that ethanol was, in  
8 fact, discussed at the meeting, and that's evidence  
9 of record that can't be denied.

10           In addition, there is testimony that many  
11 of the people who were at the meeting were there  
12 because they had a connection with ethanol.

13           ARBITRATOR ROWLEY: Isn't the evidence  
14 that's before us benign on that point?

15           MR. DUGAN: The evidence before you is  
16 benign. There is no express evidence that there  
17 was any type of agreement and we don't assert that  
18 there is any evidence in the record to that effect,  
19 but there is evidence that there were discussions  
20 of ethanol and that many of the participants who  
21 were at the meeting had fairly clear connections to

1 ethanol, and ethanol only. Mr. Listenberger, for  
2 example.

3           Seventh, after the meeting, ADM did,  
4 indeed, decide to support Davis, and they gave him  
5 a hundred thousand dollars in 1998, and at least  
6 another 50,000 in 1999.

7           Eighth, other than ADM's obvious desire  
8 and Mr. Vind's express desire to expand the use of  
9 ethanol in California, there is no apparent link  
10 between Davis and ADM. ADM is an Illinois company.  
11 It's not a constituent of anyone in California. I  
12 don't believe it had any ethanol plants in  
13 California.

14           This was similar to Vind's approaching  
15 Torricelli. Vind was a California businessman who  
16 approached a New Jersey politician to give him  
17 help. It's the same thing here. You've got an  
18 Illinois corporation, a Midwest-centered  
19 corporation approaching a California corporation  
20 seeking help.

21           Now, did Davis take steps to benefit

1 ethanol? Well, indeed, he did. First of all, he  
2 banned MTBE.

3           Second, and more importantly, he  
4 precipitously decided to use ethanol as its  
5 replacement.

6           Now, the U.S. doesn't dispute that the  
7 evidence shows that Davis ignored all the other  
8 potential oxygenates and decided upon ethanol. You  
9 saw the list, the EPA list, Caldwell's list. None  
10 of those, there is no evidence, not a shred of  
11 evidence that Davis considered anything except  
12 ethanol.

13           And the most important step he took when  
14 he issued the Executive Order in addition to  
15 banning MTBE was to order California to evaluate  
16 ethanol as a substitute. That was the only  
17 oxygenate that he ordered California to initiate a  
18 study of and paid for this type of multimedia study  
19 in order to see whether ethanol would be  
20 appropriate. None of the other potential  
21 oxygenates did he order a similar study of.

1           ARBITRATOR ROWLEY: Can you just help me  
2 on this point. I cannot recall the evidence about  
3 the UC report.

4           Was there reference in the UC report  
5 concerning the possibility of the use of ethanol as  
6 a substitute oxygenate for MTBE?

7           MR. DUGAN: There was, but I think the  
8 thrust of the UC report, as I think one of the  
9 experts, I think it was Dr. Fogg, testified to was  
10 that they recommended that the oxygenate be removed  
11 from RFG completely and that it be replaced with  
12 toluene. They did consider the possibility of  
13 replacing MTBE with ethanol, but they cautioned  
14 very, very strongly that it wouldn't be appropriate  
15 until all the adequate studies were done because  
16 they were cognizant of the potential impact, the  
17 cancer impact, the air quality impact, and the  
18 unknown impact on groundwater.

19           So, they cautioned very strongly not to  
20 use ethanol unless a complete study was done.

21           ARBITRATOR ROWLEY: Stopping you there, we

1 have two competing possible theories. One is that  
2 after election Davis decides to recommend a ban of  
3 MTBE, and its possible replacement with ethanol and  
4 orders a study of ethanol, as recommended by the UC  
5 report. The other competing theory is that he does  
6 so not because of recommendation in the U.S.  
7 report, but because of corruption having received  
8 the contribution.

9           How do we balance those two competing  
10 theories, one being a corruption theory and the  
11 other being a theory as I described following of  
12 the UC recommendations?

13           MR. DUGAN: Again, I think it's a  
14 combination of all the facts and circumstances.  
15 But I think the first question is why did he select  
16 only ethanol? There were many other oxygenates  
17 that could have been used, and, in fact, Senate  
18 Bill 521 identified a number of other oxygenates  
19 that the UC, University of California was intended  
20 to study as possible replacements. But Governor  
21 Davis did not order a study of any of them except

1 for ethanol.

2           The UC-Davis report didn't tell him to  
3 only study ethanol, but there was absolutely--there  
4 is no evidence in the record as to why Governor  
5 Davis selected only ethanol to be studied. And why  
6 Governor Davis selected only ethanol to start the  
7 process of creating, to continue the process, to  
8 jump start the process of creating an in-state  
9 California ethanol industry. And that's a critical  
10 fact, that he selected ethanol and only ethanol to  
11 receive this obvious benefit, and didn't select  
12 methanol, didn't select any methanol blend, didn't  
13 select TAME or DIPE or any of the others. Not even  
14 the ones that the Senate had ordered the UC to  
15 evaluate.

16           Now, with respect to the waiver request,  
17 there are, I think, two pieces of evidence that  
18 it's important for the Tribunal to focus on. When  
19 he made his decision banning ethanol--I mean,  
20 banning MTBE and ordering the study of ethanol and  
21 ordering steps to be taken to create an in-state

1 ethanol industry, he also included the waiver  
2 request. But I would like to go back to a slide  
3 that we put up before because I think there is some  
4 focus there, there's some evidence there that the  
5 Tribunal should focus on. And this is Tab 9 in the  
6 books that you have.

7           One final aspect of an oxygenate waiver  
8 bears emphasis. Even without a waiver of the  
9 Federal RFG oxygen mandate, a significant portion  
10 of California gasoline would still contain ethanol.  
11 There is supposed to be a period there. That  
12 emphasis is in the original, but go on to the next  
13 phrase: The MathPro analysis indicates that from  
14 cost savings perspective, the optimal share of  
15 nonoxygenated CaRFG would be less than 50 percent.  
16 Moreover, ethanol would still be needed to meet the  
17 continuing requirement for oxygenated gasoline in  
18 the winter in the greater Los Angeles area.

19           So, from this, I think the only inference  
20 is that Governor Davis intended that oxygenate,  
21 that ethanol, as an oxygenate, would receive half

1 the market in California, and I think that was an  
2 effort by Governor Davis to split the baby, but I  
3 think that Mr. Vind testified with respect to that  
4 as well, and corroborated what I speculated on in  
5 response to your question, Professor.

6 Mr. Vind testified--Mr. Vind  
7 testified--Governor Davis, and I'm going up to the  
8 top of page 10, which is page 969 from the  
9 transcript, line 4 I believe:

10 If Governor Davis banned MTBE, that  
11 would expand the use of ethanol, wouldn't  
12 it?

13 That is true.

14 Did you talk to Governor Davis about  
15 that at the meeting?

16 I did not.

17 Did you ever talk to him about that?

18 I only talked to him after the fact,  
19 after he was elected Governor, when, at a  
20 birthday party held in his honor he came  
21 over to me and asked that I intercede with

1           the oil companies and the ethanol  
2           producers to try to see if some  
3           accommodation could not be reached so that  
4           there would not be shortages of gasoline  
5           supply in the state of California, which  
6           was his fear.

7                     And what did you do? Did you act  
8           upon that request?

9                     I, in fact, did. I went to the  
10          Secretary of CalEPA, contacted at least  
11          one chairman of one major oil company, and  
12          I contacted people at ADM and some other  
13          suppliers of ethanol to try to see if I  
14          couldn't negotiate some type of compromise  
15          that would allow for perhaps some type of  
16          shifting where the refiners could, in  
17          fact, comply with Federal law. Federal  
18          law requires the addition of oxygen to  
19          gasoline in a--nonattainment areas. So,  
20          the refiners in California were concerned  
21          about not so much the use of ethanol, but

1           whether they had to be refinery-specific  
2           or whether it had to be throughout the  
3           entire state. So, that was the thrust of  
4           my conversations in my meetings.

5           Now, he dates that as Governor Davis's  
6   birthday after he was elected, and he later said he  
7   was uncertain about the date, and that it was  
8   after, substantially after the time when he was  
9   elected. But I submit that it was on December 26,  
10   which was Governor Davis's birthday, and it was in  
11   the time period between the time Governor Davis was  
12   elected and the time the ban went into place, and  
13   that this request for compromise reflects precisely  
14   what the Governor adopted. He gave half the market  
15   to ethanol and the other half of the market, the  
16   refiners were intended to be able to meet that with  
17   the production of RFG without oxygenates, which is  
18   why he asked for the waiver.

19           So, I think this is corroborating  
20   testimony of precisely the type of political  
21   compromise that politicians often enter into, an

1 allocation of the market to a favored interest  
2 without at the same time disrupting the supply  
3 economics for the citizens of California.

4           Now, the next piece of evidence is  
5 October of 1999, when Davis tells Congress that  
6 ethanol will be the replacement for MTBE, and if we  
7 could look at a time line we prepared, and that is  
8 Tab 11, November 3rd, Davis elected Governor.  
9 December 26th, the date that we believe Davis and  
10 Vind discussed the compromise. January 4th, Pete  
11 Wilson, who was an opponent of ethanol, leaves  
12 office. Davis is sworn in. March 25th, Davis bans  
13 MTBE, asks for the RFG waiver, asks for an ethanol  
14 study, and again, a study of ethanol and only  
15 ethanol, and attempts to jump start the California  
16 ethanol industry. In October of 1999, Kenny of the  
17 California Air Resources Board, testifies to the  
18 United States Senate on behalf of Governor Davis  
19 that after MTBE is eliminated, the only feasible  
20 oxygenate will be ethanol.

21           Well, how did he know that? There had

1 been no evaluation of any other oxygenate. There  
2 had been no attempt to evaluate any other  
3 oxygenates. This was, quite obviously, a  
4 precipitous decision to embrace ethanol without any  
5 consideration of the possible advantages of any  
6 other oxygenate.

7           Now--and this statement was made before  
8 the evaluations had been completed. 1999, CalEPA  
9 issues a partial health and environmental  
10 assessment of the use of fuel as an oxygenate.  
11 February 15th, 2000, CalEPA issues an addendum to  
12 its December 1999 study.

13           October 2001, CalEPA issues the final  
14 portion of the environmental assessment on the use  
15 of ethanol as a fuel oxygenate, the subsurface fate  
16 and transport of gasoline containing ethanol. And  
17 that's the one that shows that, in fact, ethanol  
18 does have a very damaging impact on the water  
19 because it increases benzene plumes by up to  
20 150 percent.

21           But the key here is that you have these

1 series of decisions favoring ethanol and announcing  
2 to Congress that ethanol will be the replacement  
3 for MTBE before any evaluation has been completed.  
4 That, in combination with the fact that only  
5 ethanol was selected for evaluation, we submit, is  
6 very strong evidence, compelling evidence, of  
7 favoritism towards ethanol, favoritism that's not  
8 justifiable on any environmental grounds.

9           Now, thereafter, California took specific  
10 steps to accommodate ethanol, steps that it did not  
11 take in any way to accommodate methanol or any of  
12 the other oxygenates.

13           Let me back up for a second. Let me go  
14 back to this December 1999 CalEPA study. Again,  
15 this was two months after Kenny had announced to  
16 Congress that the only feasible oxygenate would be  
17 ethanol. In the 1999 study, acknowledged that  
18 there were very, very significant gaps in CalEPA's  
19 knowledge with respect to what ethanol would do to  
20 the environment. And I think it's useful to focus  
21 on those gaps in knowledge because they signify

1 that CalEPA was not satisfied that ethanol would be  
2 environmentally benign.

3           As a result of the assessment contained in  
4 this volume, we have identified important knowledge  
5 gaps regarding the anticipated environmental  
6 behavior of gasoline containing ethanol. This  
7 Chapter summarizes those knowledge gaps and  
8 provides recommendations for future research that  
9 would improve decision making regarding the use of  
10 ethanol in oxygenated and reformulated gasolines in  
11 California. One of the most critical knowledge  
12 gaps is the nature of the interaction of  
13 groundwater and the air multiphase flow with  
14 ethanol containing gasoline in unsaturated zone.  
15 Understanding this process is crucial because  
16 knowledge gaps about the early states of overall  
17 flow and transport make adequate prediction of the  
18 important impacts of ethanol on BTEX contamination  
19 difficult. BTEX stands for benzene, toluene,  
20 ethylene, and, I believe xylene. So, that's the  
21 issue. They didn't know what was going to happen

1 to benzene.

2           And then you have on the next page, three  
3 more quotes from the 1999 study again identifying  
4 very significant gaps in the knowledge with regard  
5 to ethanol, and they ordered another study and the  
6 final study wasn't completed until October of 2001,  
7 and that's the next page, chart--Tab 13. Modeling  
8 results indicate a possible fourfold decrease in  
9 the mean benzene biodegradation rate as a  
10 consequence of ethanol biodegradation and  
11 associated electron receptor depletion. This could  
12 potentially increase benzene plume lengths by a  
13 factor of 2.5.

14           So, once the multimedia evaluation was  
15 finished, it turns out that ethanol may not be any  
16 better for the water than MTBE. That didn't stop  
17 Governor Davis. He'd long since decided to shift  
18 to ethanol prior to the completion of these  
19 studies, and long after deciding that only ethanol  
20 would be studied.

21           And if you remember, one of the quotes

1 that we put up, and I don't have it readily to mind  
2 so I'll just try to draw your attention to it, was  
3 a statement from, I think either Gordon Schremp or  
4 Walter Hickcox in which he said that the detects of  
5 MTBE are way down, but there is no chance they are  
6 going to repeal the ban because there was too much  
7 political momentum behind it. And Methanex submits  
8 that the political momentum there was that Governor  
9 Gray Davis was intent on favoring ethanol. He was  
10 intent on ignoring all alternatives to ethanol, and  
11 he was intent on doing so until he received some  
12 type of devastating criticism after the fact from  
13 the environmental evaluators. And all of that  
14 shows, again, an intent to favor ethanol.

15 Now, additional evidence of intent to  
16 favor ethanol is how California accommodated  
17 ethanol but not methanol. There was testimony from  
18 Mr. Fogg, Dr. Fogg, this page 1285, line 4:

19 Is it your testimony that the  
20 increase in the oxygen capped at 3.7 was  
21 not done in part to accommodate the

1           addition of ethanol?

2           The reason for doing so was to  
3           accommodate the ability of refiners to  
4           blend ethanol at 10 percent.

5           Now, would sell other oxygenate such  
6           as methanol have required the same type of  
7           accommodation?

8           Probably so.

9           I'm going to Burke's testimony. It starts  
10          on page 1437, line 18.

11          You state informal discussions with  
12          refiners and suppliers of splash blending  
13          systems did not produce a clear answer as  
14          to whether methanol can be used in the  
15          same systems that have been--that have  
16          been installed for methanol splash  
17          bending.

18          That's correct.

19          So, Burke is testifying that he doesn't  
20          know.

21          PRESIDENT VEEDER: Pausing because we'll

1 have a problem I think in a month or so. That was  
2 page 1347.

3 MR. DUGAN: I'm sorry. That was page--no,  
4 1437, 1437 starting at line 18, carrying over to  
5 1438, lines one, two, and three.

6 PRESIDENT VEEDER: I got it. Thanks.

7 MR. DUGAN: And then at the bottom of  
8 1438, line 20:

9 But if the gasoline base stock was  
10 adjusted to accommodate methanol's pure  
11 effect on the RFVP--and this is going over  
12 to 1439--the resulting gasoline would not  
13 be out of compliance with the RFG  
14 provisions; is that correct?

15 If refiners put in the extra  
16 investment and changes needed to make the  
17 more difficult underapplying blend stock  
18 that I feel would be needed to blend in  
19 methanol, that's correct. And they could  
20 do it. There is no question about that.  
21 So, the same types of accommodations could

1 have been made for other oxygenates, but they  
2 weren't. They were made only for ethanol.

3 ARBITRATOR ROWLEY: Mr. Dugan, you make  
4 your case turn on the contributions that were made  
5 by ADM and the ethanol industry to Mr. Davis. Is  
6 there evidence before us, or do we have knowledge  
7 as to whether methanol producers and/or Methanex  
8 made contributions to Governor Davis or his  
9 predecessor?

10 (Pause.)

11 MR. DUGAN: I'm not sure.

12 I'm not sure. I'm frankly not certain  
13 what the evidence is in the record. I think there  
14 is evidence of one contribution by Methanex that  
15 was rejected because Methanex is a Canadian  
16 corporation, and it's not allowed under U.S.  
17 campaign contribution laws to make contributions.  
18 That contribution was not to Gray Davis. It was  
19 not to Gray Davis or to anyone in California. The  
20 check was--I don't know whoa it was to. The check  
21 was returned, and Methanex has since adopted a

1 policy of not making any political contributions.

2 ARBITRATOR ROWLEY: Could you have one of  
3 your assistants just identify in the record what  
4 that evidence is so we can turn to it, if  
5 necessary.

6 MR. DUGAN: We'll do so.

7 ARBITRATOR ROWLEY: Thank you very much.

8 ARBITRATOR REISMAN: Mr. Dugan, the two  
9 corporations in the United States also had a policy  
10 of not making contributions?

11 MR. DUGAN: And actually--probably I  
12 should make that clear. Corporations in the United  
13 States can't make contributions, either. But  
14 corporations--

15 ARBITRATOR REISMAN: They have no PACs?

16 MR. DUGAN: I will check that.

17 PRESIDENT VEEDER: I misunderstood, then.

18 In paragraph 178 of the United States Amended  
19 Statement of Defense, page 72, it's pleaded that  
20 ARCO, an MTBE producer, amongst others, made  
21 contribution to Governor Davis's campaign.

1           MR. DUGAN: We don't dispute that, that  
2 some of the refiners undoubtedly made contributions  
3 to Governor Davis's campaign. I'm sorry, perhaps I  
4 misunderstood the question. I thought the question  
5 was--the question was directed towards Methanex.  
6 If it's directed--

7           PRESIDENT VEEDER: Was the answer you gave  
8 that corporations can't make campaign  
9 contributions?

10          MR. DUGAN: Right. And I think that that  
11 is a shorthand that many newspapers use. What  
12 they're really talking about is that there's  
13 something, and I'm speculating, but I know this is  
14 done as a matter of course, there is something like  
15 an ARCO Political Action Committee, and executives  
16 in ARCO make contributions to the Political Action  
17 Committee and then the Political Action Committee  
18 actually makes contributions to particular--and  
19 that's the way it is with ADM as well, so in terms  
20 of using that shorthand, when I say that ADM made  
21 contributions, I think that those are contributions

1 from an ADM good government fund, or something like  
2 that, a Political Action Committee, as opposed from  
3 ADM itself, because it is illegal for corporations,  
4 as I understand it, to directly make contributions.

5 PRESIDENT VEEDER: Could you just help us  
6 on the pleading references and come back to it  
7 later, but it's our recollection that there is in  
8 the evidence two attempts by the Methanex U.S.  
9 subsidiaries to make political contributions which  
10 were returned because of the ownership by the  
11 Canadian parent; is that right?

12 MR. DUGAN: I don't think that is right,  
13 but let me check.

14 (Pause.)

15 MR. DUGAN: We will look up the cite, but  
16 I'm informed that what happened is that a Methanex  
17 entity, whether it was Methanex-US or Mexican  
18 Canada is unclear, made a contribution drawn on a  
19 Canadian bank, and it was rejected because it was  
20 drawn on a Canadian bank. But we are checking to  
21 find out exactly what the facts are.

1           The next point, I think that it's  
2   important to consider in this whole evaluation of  
3   the facts and circumstances surrounding it is that  
4   the question of whether ADM did, in fact, benefit  
5   from the shift to ethanol, and I think the evidence  
6   is undisputed that it did.

7           Tab 16, in 2002, as it was starting to  
8   kick in, ADM clearly benefitted--quote, We, ADM have  
9   reason to believe there is a very strong demand for  
10  ethanol across this country. We're in a strong  
11  position in the ethanol business.

12           Now, in addition to that,  
13  Mr. Listenberger, in his testimony acknowledged  
14  that ADM had benefitted, and this is from page 878  
15  and 879, starting on line 20:

16                   Will you admit that ADM's  
17                   ethanol--you admit today as you sit here  
18                   six years after having Gray Davis and five  
19                   years after the MTBE ban that ADM's sales  
20                   of ethanol increased after that ban?

21                   Yes, they did.

1           Mr. Listenberger further admitted--and  
2 this is on page 876:

3           You would agree that the ban was good  
4 for ADM's sales, wouldn't you?

5           It had the potential to be very good  
6 for ethanol sales over the entire  
7 industry, yes. In fact, ADM celebrated  
8 this ban, didn't they?

9           I thought it was a good idea, so, by  
10 thinking it was a good idea, you  
11 celebrated, didn't you?

12           I suppose in our own way.

13           So, the evidence that ADM has benefited  
14 and, in fact, celebrated when the ban was enacted,  
15 I think, is irrefutable. This was very good for  
16 ADM.

17           Now, Methanex submits that once you accept  
18 the premise that there are instances of political  
19 corruption in the United States, where again to use  
20 Senator Rudman's words, money affects outcomes,  
21 that the evidence that I have just gone through,

1 the 11 factors, all points to that conclusion here.  
2 This was an instance where ADM's money obtained  
3 favoritism for ethanol in California just as, to  
4 use Senator McCain's words, ADM traded its  
5 political contributions for the political tax  
6 credits.

7           This is very similar, identical in  
8 technique to that. That's what we believe the  
9 evidence shows.

10           And we don't think that is merely a prima  
11 facie case. We think that barring any rebuttal  
12 evidence, this is a conclusive case. Again, once  
13 you accept this premise that this type of  
14 corruption exists, this fits that pattern to a T.  
15 Why else would Gray Davis select ethanol and only  
16 ethanol for evaluation? Why else would Gray Davis  
17 announce that ethanol was the only feasible  
18 substitute when no one in California had bothered  
19 to evaluate anything else. Why else would they  
20 focus on ethanol and only ethanol as the possible  
21 replacement for MTBE?

1           The only possible reason that we could  
2 think of is because Gray Davis was doing his best  
3 to favor an interest that had contributed heavily  
4 to him.

5           Now, what's the evidence rebutting the  
6 conclusion that there was some type of implicit  
7 accommodation at the meeting? And again, go back  
8 to the circumstances of the meeting. Prior to the  
9 meeting, ADM had not decided whether to support it.  
10 After the meeting, he decided to support  
11 him--decided to support him quite heavily.

12           The evidence from Listenberger, Vind, and  
13 Weinstein are neutral with respect to what  
14 happened. Yes, there was some discussion of  
15 ethanol, but no discussion of MTBE or methanol.  
16 But it's important that each one admitted that  
17 ethanol was discussed and, more importantly, each  
18 one admitted that they didn't hear all the  
19 conversations that took place that night.  
20 Weinstein admitted it. Transcript 837, 16 to 20,  
21 839, 17 to 840, 1. That was Weinstein,

1 Listenberger admitted it, transcript 851, lines  
2 four to six, and Vind admitted it transcript 964,  
3 1 through 10.

4           Now, that brings up the question, one of  
5 the critical evidence questions in here: Why are  
6 Listenberger and Weinstein here testifying as to  
7 what happened at the meeting? Well, here is what  
8 Weinstein said. This is at page 847.

9           Well, do you honestly know why you're  
10 here? You are the witness for the United  
11 States rather than Alan Andreas?

12           I have no idea.

13           Do you know honestly why you are the  
14 witness for the United States rather than  
15 Marty Andreas?

16           I have no idea.

17           Again, what did Listenberger say? This is  
18 page 873, line four:

19           And then it's August 17, 1998, less  
20 than two weeks later that Mr. Davis  
21 received a contribution of \$100,000 from

1 ADM; is that correct?

2 I have no idea.

3 If it were true, that would indicate  
4 that ADM assessed the candidacy of  
5 Mr. Davis and decided to support his  
6 candidacy; isn't that correct?

7 Again, I would have no involvement in  
8 that type of decision. I don't know.

9 So, what have you here is a classic case  
10 of empty chairs. Where is Governor Davis? He  
11 wasn't interested in coming. Where are the  
12 Andreases? They're not here. We tried to get them  
13 here. We weren't allowed to. We submit that there  
14 is no evidence rebutting the fact that there was an  
15 implicit agreement reached at that meeting that  
16 caused ADM to decide to support Governor Davis.  
17 And the implicit agreement was reached that they  
18 would support him, and he would expand the use of  
19 ethanol, and there is no evidence rebutting that.

20 In fact, we will go one step further. The  
21 fact that this chair is empty, the fact that the

1 Andreases are not here, the inference to be drawn  
2 from that is that were they here, they would  
3 confirm this story. That's the only inference you  
4 can take from the fact that they refused to come  
5 and that the United States has blocked our attempts  
6 to get that evidence.

7           So what you have is a series of events,  
8 pieces of evidence, the totality of the facts and  
9 circumstances that point to the fact that this is,  
10 indeed, one of those cases where that type of  
11 corruption take place, and no evidence rebutting it  
12 whatsoever.

13           Now, the U.S. has raised the question of  
14 ARCO. ARCO, we submit, is in a much different  
15 situation. ARCO doesn't exist because there is a  
16 Federal tax subsidy that keeps it alive. It exists  
17 because there is a legitimate economic need for  
18 gasoline and refinery. That's not the case for  
19 ethanol.

20           Second, ARCO was a California constituent  
21 that had refineries in California and had a

1 legitimate interest in meeting with Davis.

2           Third, ARCO is not ADM. ARCO does not  
3 have ADM's notorious history of seeking out, for  
4 example, the tax credits for ethanol. ARCO is not  
5 ADM and it doesn't play the same role in the  
6 political process that ADM does.

7           Fourth, ARCO's meeting was not secret. I  
8 believe, and we weren't able to find this, but I  
9 believe that there was a public report of the  
10 refinery tour that Governor Davis or his  
11 representative took.

12           And all those--all those facts, we think,  
13 point to a much different situation between ARCO  
14 and ADM. ARCO is not ADM. ARCO may not--well,  
15 ARCO isn't ADM, and the fact that it didn't get  
16 anything in response for--in return for its  
17 contributions, ARCO has many, many different  
18 interests in California. It's a constituent in  
19 California. ADM is not. The totality of the facts  
20 and circumstances, once again, once you accept the  
21 premise, the Supreme Court's premise and Senator

1 Rudman's premise that there are times when money  
2 affects outcomes, this was one of those times.

3           Now, with respect to 1102 there are other  
4 requirements that have to be met with. The first  
5 one of those is like circumstances. And here  
6 again, it would be useful to know what the  
7 negotiating history is with respect to like  
8 circumstances. We don't know. We have one phrase,  
9 unexplicated as to which the parties differed  
10 greatly. It would be useful to know what the  
11 negotiating texts, what the various drafts said  
12 about this.

13           Now, I think there are three aspects of  
14 the like circumstances test that are worth  
15 responding to. First, I don't think there is any  
16 longer any doubt that both methanol and ethanol  
17 compete in a single unified market, and I think  
18 that the United States's economic expert,  
19 Mr. Burke, confirmed that. And this is quoting  
20 from page 1448, line two. I'm sorry, it's Tab 19.

21           Was it your testimony that the

1 gasoline supply chain is a continuous  
2 cycle rather than divided among refiners  
3 and blenders?

4 Yes, it's a continuous supply chain.

5 So, the evidence supports the chart that  
6 we put up on the day that we opened in which we  
7 showed that both ethanol and methanol are  
8 oxygenates used in the production of RFG. They're  
9 used at different points in this continuous cycle,  
10 but the cycle should be viewed in the words of  
11 Mr. Burke himself as a continuous supply chain.  
12 And the fact that the oxygenates are used at  
13 different points in this RFG production process is  
14 simply not relevant.

15 ARBITRATOR REISMAN: Excuse me, I think  
16 the record shows Mr. Burke then said that is not  
17 correct. I'm looking at line--

18 MR. DUGAN: He went on to say that it's  
19 irrelevant--what I'm pointing at, I think what he  
20 contested was the fact that it's irrelevant where  
21 the oxygenate is inserted into the production

1 process, but he agreed that it's one continuous  
2 supply cycle.

3           Now, second, there has been a lot of back  
4 and forth over the U.S. like products test. And  
5 the U.S. asserts that methanol and ethanol are not  
6 like products using the GATT/WTO test. But we  
7 believe the evidence shows that's simply not true.  
8 Both of them are alcohols. Both of them are  
9 oxygenates and both of them are used in the  
10 production of RFG as oxygenates. They are the two  
11 chemicals that produce the oxygenate in RFG or  
12 oxygenated gasoline.

13           In addition, both can be made for the same  
14 proposes. If you recall the testimony about pig  
15 manure. Both could be made in from the same basic  
16 processes, and that's another thing that supports  
17 the fact that they are like products.

18           In terms of end uses, as we've tried to  
19 show, their end use in the context of this case is  
20 identical. Both are used for precisely the same  
21 purpose because they provide the oxygenate needed

1 in RFG. The fact that they're used at different  
2 portions of the production process is wholly  
3 irrelevant.

4           Now, furthermore, in terms of the end uses  
5 what we tried to show is that the integrated  
6 companies have a binary choice. They can choose  
7 ethanol or they could choose methanol. So the end  
8 use of the products is similar or not precisely  
9 identical, but it does exist in the context of this  
10 binary choice. In fact, going back to the  
11 California regulation, the one that now bans  
12 methanol by name, it identifies it as an oxygenate;  
13 and, by implication, it identifies it as a  
14 competing oxygenate, and that's why it banned it by  
15 name, is because it's precisely the type of  
16 oxygenate that could take the place of ethanol.

17           MR. LEGUM: Mr. President, before we move  
18 on to a different subject, I would just like to  
19 note our objection to the reference to the pig  
20 manure. That was not offered as a part of  
21 Methanex's case-in-chief, and I don't believe that

1 there is any competent evidence on that subject in  
2 any event.

3 PRESIDENT VEEDER: Is there any evidence  
4 on this pig manure, Mr. Dugan?

5 MR. DUGAN: I'm sorry, I thought that was  
6 part of the record. Perhaps I'm mistaken.

7 PRESIDENT VEEDER: We had something about  
8 digested pig manure. Is this the same point?

9 MR. DUGAN: This is the same point, yes.

10 PRESIDENT VEEDER: I'm not sure that's in  
11 the evidence. I think it was a question put to the  
12 witness.

13 MR. DUGAN: Okay. Then I'll withdraw it.

14 PRESIDENT VEEDER: Please don't take it  
15 from me. If there is any evidence, I would like  
16 you to identify it to us, but come back on it later  
17 if you'd like.

18 I can also say that we have to give our  
19 shorthand writer a break within the next ten  
20 minutes or so, so when you come to a natural break,  
21 Mr. Dugan, we could take another short break.

1           MR. DUGAN: This is actually a good point  
2 to take a break.

3           PRESIDENT VEEDER: Let's take a 10-minute  
4 break.

5           (Brief recess.)

6           PRESIDENT VEEDER: Let's resume.

7           MR. DUGAN: Thank you.

8           The next point I would like go to, the  
9 next chart I'd like to go is our binary choice  
10 chart, and this is an extrapolation of the chart we  
11 put in in the opening, and I will point out that  
12 the last cite that Chairman Key's prepared witness  
13 testimony to the Committee on Government Reform is  
14 not actually part of the record. If the U.S. wants  
15 to object, it's all available at the CEC Web site,  
16 and it was used strictly to project the amount of  
17 ethanol--I mean the amount of ethanol that will be  
18 consumed in the future. And this just illustrates  
19 that in terms of--they are competing uses, that  
20 there is a binary choice and the long-term effect  
21 of what will have happened is that ethanol will

1 replace methanol completely in terms of the  
2 alcohols that are used as oxygenates in California  
3 in the manufacture of RFG.

4           Now, turning to the next prong of the  
5 like-products test, consumer preferences, the  
6 consumer preferences analysis which was used in  
7 asbestos, does not support the United States here.  
8 But before we get into it, I think it's appropriate  
9 to point out that most WTO cases use the--do not  
10 analyze the question of an environmental  
11 justification in the context of consumer  
12 preferences or likeness. That's usually done at  
13 the stage after it's been established that there  
14 are like products and there is a denial of national  
15 treatment. At that point it then becomes the  
16 burden of the respondent state to justify the  
17 purported environmental justification for a  
18 measure. And we think that's the appropriate way  
19 for this Tribunal to view it procedurally as well,  
20 to place the burden on the United States Government  
21 to justify the ban of methanol and, more

1 importantly, the shift to ethanol as a responsible  
2 environmental measure.

3           But taking the consumer preference test at  
4 face value, the first point to be made here is  
5 that--and the consumer preferences comes out of the  
6 asbestos case, but the first point to be made here  
7 is that the consumers here are not consumers of  
8 gasoline. They're not families that buy from gas  
9 pumps. The consumers here of these oxygenates,  
10 these competing oxygenates, are the integrated oil  
11 companies and the gasoline blenders, the ones who  
12 switched from methanol to ethanol or from MTBE to  
13 ethanol. Those are the consumers, not individual  
14 drivers.

15           And it's quite clear that their preference  
16 prior to the mandated ban was for MTBE and for  
17 methanol, respectively. Those were their  
18 oxygenates of preference. They dominated the  
19 market, and they dominated the market for a number  
20 of well-known reasons. So, if consumer preferences  
21 are to be important, they showed no preference for

1 ethanol whatsoever.

2           Now, even if were appropriate at this  
3 stage of the analysis to factor into the  
4 environmental and the health factors, again that  
5 doesn't help the United States. It hurts the  
6 United States, especially at the time that the ban  
7 was implemented and the shift to ethanol was made.

8           Now, recall that in the asbestos case, the  
9 competing products were different types of  
10 asbestos, one of which was far more benign than the  
11 others, think it's called crysolite (sic). So,  
12 there was a very clear difference between the two  
13 categories of asbestos in that case. The case here  
14 is that especially in 1999, it was well-known that  
15 ethanol far more dangerous to the environment and  
16 to health than methanol was. That didn't stop  
17 California from shifting to it.

18           Let's start with--go to the evidence.  
19 What was the evidence? What was known about  
20 ethanol's effect at the time that the shift was  
21 made? Well, and we put this up before. Under Pete

1 Wilson, Governor Davis's predecessor, California  
2 had objected to the use of ethanol, and they'd  
3 objected to it on health and environmental grounds.  
4 The first one, again, was the veto message that  
5 Governor Wilson sent to the California Legislature  
6 when he vetoed a previous attempt to benefit  
7 ethanol. And one of the reasons why he vetoed it  
8 is that the last phrase of his veto statement,  
9 "especially when the consequences will foul our  
10 air." He was talking about ethanol.

11           Prior to that, when the EPA had attempted  
12 to implement a 30 percent set aside for ethanol,  
13 California had sued, and again he had sued on the  
14 grounds that the ethanol mandate would result in  
15 irreparable injury to the health and welfare of  
16 California citizens and to the environment.

17           So, prior to this ban and shift to  
18 ethanol, California did not believe that ethanol  
19 was a better product. In fact, they thought it was  
20 quite clearly a worse product.

21           Now, similarly, even at the time when

1 Davis made the shift to ethanol, the record in the  
2 case showed that ethanol could have some very, very  
3 damaging consequences, and what we have plucked out  
4 for you is the portion of the California report.  
5 This is the UC-Davis report itself that identifies  
6 the cancer risks of increased ethanol. And if you  
7 look at the third column, it says acetaldehyde, and  
8 footnote three, footnote three if you go to the  
9 next page refers to due to ethanol.

10           And if you go all the way to the bottom of  
11 page eight of Tab 22, you will see the reference  
12 that we have used repeatedly. Statewide change in  
13 cancer cases, acetaldehyde due to ethanol 38 to  
14 2,800 additional statewide cases of cancer. That's  
15 what the UC-Davis report identified as the  
16 carcinogenic impact of switching to ethanol at this  
17 time.

18           And when Davis decided to evaluate only  
19 ethanol and when he decided in October of 1999 that  
20 ethanol was the only feasible alternative, this was  
21 the operative science, up to 2,800 additional cases

1 of cancer. And the citation to that, that's  
2 40 JS tab G is the original record for that.

3           Similarly, we also put up before the slide  
4 from the October 2001 report that showed that  
5 shifting to ethanol is going to substantially  
6 increase the benzene risk, the risk of benzene  
7 contamination. So, I don't think it can ever be  
8 reasonable be said, especially in 1999, the time  
9 that the shift was made, that methanol--that MTBE  
10 was a more dangerous product than ethanol. The  
11 cancer risk alone defies that conclusion.

12           Now, the third point about like  
13 circumstances that I think is useful to evaluate  
14 are the Pope and Talbot and the Feldman cases. We  
15 don't read them the same way as the United States  
16 does, not surprisingly. But we think in Feldman  
17 that there wasn't any evidence in Feldman that the  
18 Mexican cigarette manufacturers were competing with  
19 the cigarette resellers. There was an absence of  
20 evidence to that effect. And in Pope and Talbot,  
21 the competitive circumstances between Pope and

1 Talbot's Canadian subsidiary and lumber companies  
2 in the other provinces was much different  
3 competitively because Pope and Talbot was in one of  
4 the provinces that was subject to a countervailing  
5 duty which triggered the whole quota system, and  
6 the other one wasn't. So the nature of the  
7 competition, if it existed at all, was much, much  
8 different, and for that reason, we don't think that  
9 the two cases serve as a useful precedent.

10 I'm sorry, the previous citation to the  
11 cancer chart I'm told is five JS tab 40 G.

12 Now, if under Methanex's analysis  
13 it--methanol and ethanol are in like circumstances,  
14 then I think it's quite clear that methanol didn't  
15 receive the same treatment as ethanol, and I won't  
16 go over that again. It has lost its California  
17 market. It's not entitled to sell ethanol as an  
18 oxygenate to RFG producers. And I think at this  
19 stage the burden shifts to the United States to  
20 justify the ban on MTBE and the precipitous shift  
21 to ethanol as a serious and valid environmental

1 measures, and I don't think they can do that.

2           We have just gone through some of the  
3 cancer issues. We have just gone through some of  
4 the water treatment issues, of the finding by  
5 California itself that the use of ethanol poses a  
6 very serious benzene risk to the drinking water of  
7 California, which is itself already a more serious  
8 risk than even by in the words of the United  
9 States's own expert, benzene is more serious risk  
10 than MTBE, and shifting to ethanol will only  
11 increase that risks.

12           But in addition to those, what is the  
13 other scientific evidence? We've put a lot in and  
14 there is a lot there, and I would like to pluck out  
15 a few highlights of the scientific evidence. First  
16 of all, was MTBE a good product? And this is just  
17 going to Dr. Fogg's testimony, page 1274, line 14.  
18 And while, line 18:

19                   While MTBE was the oxygenate of  
20                   choice in 1996, the Phase II program  
21                   reduced emissions of hydrocarbons by

1 17 percent; correct?

2 That is correct.

3 And it reduced the emissions of  
4 oxides of nitrogen by 11 percent; correct?

5 That is correct.

6 And during that same time period in  
7 1996 when MTBE was the oxygenate of  
8 choice, carbon monoxide emissions were  
9 reduced by 11 percent; is that correct?

10 That is correct.

11 And during the same time period  
12 sulfur oxides were reduced by 80 percent;  
13 is that correct?

14 That is correct."

15 I'm sorry, that was Simeroth, not Fogg.

16 Again, pages 274 and 1275. So, I think it's--and  
17 that's the United States's own expert.

18 It's absolutely unquestioned that  
19 methanol--that MTBE was a very effective pollution  
20 reducer.

21 Now, with respect to one of the critical

1 scientific issues, I'd like to read from the  
2 Exponent report that's at 12 A, JS Tab C. And the  
3 summary there I think is the most important aspect  
4 of it. In summary, the UC report significantly  
5 mischaracterized the then-current impacts of  
6 drinking water sources and their prediction of  
7 substantially increased incidence and levels of  
8 MTBE detected in drinking water sources over time  
9 has not materialized. And we haven't put it back  
10 up again, but just recall that when Governor Davis  
11 extended the time period for the total ban on MTBE,  
12 in his Executive Order, he himself said that the  
13 detections of MTBE had decreased substantially. I  
14 think Walter Hickox and Gordon Schremp also stated  
15 that the detections of MTBE had decreased  
16 tremendously.

17           So in California's own words, the words of  
18 their own officials validate what Dr. Williams has  
19 said. During the period between 1999 and the time  
20 when the ban went into effect, MTBE detects in  
21 drinking water dropped tremendously or

1 substantially.

2 She goes to state:

3 On the contrary, the incidents of  
4 MTBE in drinking water sources statewide  
5 was relatively low in 1998 and has not  
6 increased over time. The importance of  
7 this inaccurate assessment cannot be  
8 overstated because in the absence of  
9 adverse ecological effects, it appears to  
10 have been the sole basis for the  
11 Governor's finding of a significant risk  
12 to the environment.

13 Now, you heard from Dr. Happel, and she  
14 came in and she talked about 10,000 points of water  
15 polluted by MTBE. And I think that's telling  
16 because that's an example of the type of gross  
17 exaggeration that has accompanied this whole  
18 debate.

19 And I'm turning to page 1163, line 11, of  
20 Happel's testimony, and in her answer:

21 I'm looking to say in your database

1           that the State Water Board--how many of  
2           the leaking tank sites that have been  
3           tested for MTBE have found MTBE in  
4           groundwater pollution in the groundwater?

5           And the answer is 10,000.

6           And the question:

7                     When you talk about groundwater  
8           pollution you're not looking at the MCL  
9           level; correct?

10                    No, this is anything above one part  
11           per billion.

12                    So it's any detect; correct?

13                    Yes.

14                    So, again, this 10,000 is based upon  
15           detects, most of which, the majority of which were  
16           of no concern to anyone. They are below the MCL  
17           for esthetic threshold and they're below the MCL  
18           for health. Nonetheless, it was the figure that  
19           was bandied about, and it did create an awful lot  
20           of hysteria.

21                    Dr. Happel also admitted, and this is

1 page 1260 line 20:

2               So, if you use the detect frequency  
3               method rather than the cumulative detect  
4               method, your charts would look different  
5               today, wouldn't they?"

6               She conceded that the charts would look  
7 different.

8               Testimony went on, page 1263, line 20:

9               In your conclusion, the 3 percent of  
10              the sources that you study were  
11              contaminated by MTBE; is that a correct  
12              statement of your findings?

13              No, we estimated the number of public  
14              supply wells that may have been  
15              contaminated using inadequate data. We  
16              came up with a range of .3. I think  
17              that's meant to be 1.2 percent of supply  
18              wells.

19              So, even by Dr. Happel's own admission  
20              with respect to drinking water sources, it was a  
21              very, very small percentage.

1           And similarly, no one now disputes that,  
2 as we said in the opening, the UC-Davis study  
3 bungled the estimate of the cost of cleanup.  
4 Whitelaw himself candidly admitted that. And going  
5 to page 1527:

6           QUESTION: Let me return to your  
7 analysis of the UC report and the errors  
8 you attribute to it. On page three of  
9 your original report you concede that the  
10 authors of the UC report erred by  
11 including so-called sunk costs in the  
12 water quality analysis; correct?

13           I concede?

14           You contend.

15           I observed. Everyone else had  
16 observed that before I got the report.  
17 Well, not everybody, but I mean a number  
18 of people.

19           So, it was a blatant and serious error.

20           And finally, with respect to I think one  
21 of the most important questions, was this the most

1 suitable choice for California to make, again,  
2 recall that the language of SB521 required Governor  
3 Davis to take appropriate choice. Didn't tell him,  
4 didn't require him to ban MTBE. And the fact that  
5 it contemplated MTBE ban as a possibility in no way  
6 means as a matter of legislative intent that he was  
7 required to ban MTBE.

8           Now, the United States tries to make it  
9 out as if that were the only realistic choice.  
10 That's wrong. It wasn't the only realistic choice,  
11 and he was under no requirement whatsoever to ban  
12 the MTBE, and he certainly wasn't under any  
13 requirement to substitute ethanol without having  
14 adequately studied it, which is what he did. But  
15 going back to the testimony with respect to a more  
16 suitable measure, more appropriate action to  
17 protect the environment, Dr. Fogg admitted that  
18 banning the two-stroke engine would solve the  
19 problem--

20           ARBITRATOR ROWLEY: Could I just ask you a  
21 question here. I think you said that Governor

1 Davis banned the use of MTBE before completing the  
2 study of ethanol.

3 MR. DUGAN: No. What I meant to say  
4 was--if I said that, I misspoke.

5 What I have been trying to say is that  
6 Governor Davis decided to substitute ethanol as the  
7 replacement for MTBE before California had  
8 completed not only the evaluation of ethanol, but  
9 any comparative evaluation of any other oxygenates.  
10 That's the critical decision that he made. That's  
11 the second critical decision he made was to select  
12 ethanol and to select it on a final basis, which is  
13 what he told Congress, before the ethanol-specific  
14 evaluation had been completed:

15 But more importantly, to select ethanol as  
16 the only oxygenate to evaluate. And to ignore all  
17 the other potential oxygenate competitors. That's  
18 the important part of the process, the two-step  
19 process, first ban MTBE; second, select ethanol  
20 preferentially over all its competitors.

21 Does that answer the question?

1           Now, turning to Fogg's testimony, this is  
2 page 1265, line 16:

3           And you would agree that by  
4 preventing the use of a two-stroke engine,  
5 you're preventing the release of gasoline  
6 from the two-stroke engine into the lake?  
7 You are taking the source of MTBE out of  
8 the water body?

9           Yes.

10          So, Dr. Fogg agreed that that was an  
11 appropriate solution for solving the surface water  
12 problem and that, in fact, was the solution that  
13 was adopted.

14          Similarly, Dr. Happel, page 1202:

15          So, banning MTBE doesn't stop  
16 gasoline release into the groundwater; is  
17 that correct?

18          Banning MTBE does not affect the  
19 ability of the UST tank, the underground  
20 storage tank, to prevent releases.

21          Dr. Happel, page 1196, line three:

1                   And you would agree that if less  
2                   gasoline is released into those  
3                   groundwater sources, that would be less  
4                   contamination of any kind; is that  
5                   correct?

6                   Yes.

7                   Now, at the hearings that took place after  
8                   the report was issued, there was a particularly  
9                   eloquent statement from one of California's water  
10                  officials, and this is found at Tab 26, and this is  
11                  a statement from Bill Robinson, the Director of the  
12                  Upper San Gabriel Water District Division Number  
13                  Four. He testified that, quote, The ancient  
14                  Egyptians had the technology to preserve corpses  
15                  for thousands of years, and our state Legislature  
16                  can't give us underground storage tanks that don't  
17                  leak. That's the solution to the problem. If the  
18                  Legislature will fund that, the underground storage  
19                  tank program, they can avoid billions of dollars in  
20                  cleanup costs. Just avoid the costs. It's a  
21                  no-brainer decision to make.

1           That was a California water official who  
2 repeated what Methanex believes is the obvious  
3 conclusion that should have been reached.

4           PRESIDENT VEEDER: Can you just give us  
5 the reference in the exhibit bundles?

6           MR. DUGAN: We'll find it and  
7 cross-reference it to the exhibit bundles.

8           So, we think that reviewing the whole  
9 national treatment issue, the four points, first of  
10 all, we think it's especially because of the  
11 competitive relationship between ethanol and  
12 methanol that they are, indeed, in like  
13 circumstances.

14           Secondly, that methanol does not receive  
15 the same competitive opportunities that ethanol  
16 does because it can't sell methanol as an oxygenate  
17 in California to RFG manufacturers.

18           And third, that the U.S. cannot justify  
19 both the MTBE ban and the shift to ethanol on an  
20 environmental basis. The record to do that simply  
21 isn't there, especially the shift to ethanol. It

1 can't be justified as an environmental measure.

2           Now, with respect to our allegations of  
3 corruption, that is not necessary to prove an 1102  
4 violation. We have offered that evidence because  
5 we believe that that conclusively explains why 1102  
6 was violated. It explains why Governor Davis took  
7 the acts that he did, but that proof is not  
8 necessary. All we have to prove is like  
9 circumstances, disparate treatment, and that the  
10 United States cannot meet its burden to justify the  
11 ban and the shift to ethanol as an environmentally  
12 sound measure.

13           Once we prove those three things, Methanex  
14 believes it has proved a violation of 1102,  
15 regardless of whether the Tribunal was satisfied  
16 that it was done for corrupt purposes.

17           Now, the cross-reference citation for the  
18 Egyptian mummy quote that I just read you is  
19 11 JS Tab 2 01.

20           Now, turning to Article 1105, fair and  
21 equitable treatment, Methanex proffered Professor

1 Crawford's synthesis of fair and equitable  
2 treatment because Methanex submits that this is  
3 compelling evidence of the present state of  
4 customary international law of fair and equitable  
5 treatment. It's what the customary law is now.  
6 The waste management decision came after the FTC  
7 alleged interpretation of 1105, and it took that  
8 into account. It factored that into account.

9           Professor Crawford noted that customary  
10 international law is an evolving standard. He  
11 noted that the parties, the NAFTA parties had  
12 agreed that is an evolving standard, and taking  
13 into account all the developments in development of  
14 the concept of fair and equitable treatment, this  
15 was how he had--this was how he did articulate the  
16 present content of the fair and equitable standard,  
17 and we believe that this is as concise and as  
18 persuasive an articulation of that standard as  
19 exists anywhere.

20           ARBITRATOR REISMAN: The reference in  
21 Professor Crawford's statement or award to

1 discriminatory treatment is what equalizes, that  
2 makes the evidence that you marshalled with respect  
3 to 1102 relevant to 1105.

4 MR. DUGAN: That's one of the headings,  
5 not the only heading, and I will get to that, if I  
6 can.

7 ARBITRATOR REISMAN: But that is why the  
8 evidence that you marshalled of 1102 is relevant to  
9 1105? There may be other evidence?

10 MR. DUGAN: Yes, with the same evidence  
11 that I think supports 1102 supports a violation  
12 under 1105, a number of different headings, one of  
13 which is discrimination.

14 But turning to exactly what Professor  
15 Crawford said, he refers to conduct that is  
16 arbitrary, grossly unfair, unjust, or  
17 idiosyncratic. And we submit that what happened in  
18 California was precisely that, that whenever a  
19 political official implicit return for political  
20 contributions favors one competitor and shuts  
21 another competitor out of the market, that that's

1 arbitrary, it's grossly unfair, it's unjust, and  
2 it's idiosyncratic because it's a policy decision  
3 that's made not on the merits of the underlying  
4 situation, but because of a desire to favor one  
5 particular interest, an interest that had  
6 contributed to that person.

7           Similarly, it's discriminatory for the  
8 reasons that we just talked about.

9           Now, the United States has said there is  
10 no general rule against discrimination. I submit  
11 that the way that Professor Crawford has  
12 articulated the current state of the law, with  
13 respect to fair and equitable treatment that some  
14 forms of discrimination are, indeed, illegal under  
15 international law. They are unfair, and they are  
16 inequitable. And we further submit that the type  
17 of discrimination that Methanex faced in California  
18 at the hands of Gray Davis is precisely that type  
19 of discrimination that is illegal under the fair  
20 and equitable treatment standards.

21           ARBITRATOR REISMAN: You stated some forms

1 of discrimination are violations of international  
2 law. You mean violations of customary  
3 international law?

4 MR. DUGAN: Violations of the fair and  
5 equitable standard that is included as an express  
6 textual pretension in Article 1105.

7 ARBITRATOR REISMAN: Let me make sure I  
8 understand. 1105, this interpretation liberates  
9 1105 from customary international law. Just look  
10 at the words fair and equitable. And you derive  
11 from it that discrimination would be a violation of  
12 fair and equitable treatment. It doesn't take you  
13 back to customary international law.

14 MR. DUGAN: I think it may take you back  
15 to customary international law. I'm not quite sure  
16 how Professor Crawford articulated the link between  
17 this articulation and customary international law  
18 and whether he fully accepted the FTC  
19 interpretation that it was wholly dependent on  
20 customary international law.

21 ARBITRATOR REISMAN: It's your position

1 that a state may not discriminate between national  
2 and aliens under customary international law?

3 MR. DUGAN: It's certainly our position  
4 that a state may not discriminate on the facts of  
5 this case between an alien and a domestic interest  
6 because of political contributions, that that is a  
7 violation.

8 ARBITRATOR REISMAN: I don't think that  
9 addresses the problem the Tribunal had with 1105.

10 First, does--if 1105 incorporates  
11 customary international law, does customary  
12 international law prohibit a state from treating  
13 aliens and its own nationals differently?

14 MR. DUGAN: I think it depends on the  
15 circumstances. I don't think that there is a  
16 blanket prohibition, and I think again, in some  
17 circumstances, it does prohibit it.

18 ARBITRATOR REISMAN: Can you give us  
19 authority for, international authority for  
20 circumstances in which it has been held that  
21 customary international law prohibits differential

1 treatment?

2 MR. DUGAN: No, I can't, not offhand, but  
3 I mean in terms of authority that customary  
4 international law prohibits discriminatory  
5 treatment, I think this is evidence of it, the fact  
6 that it is articulated, as including discrimination  
7 is itself evidence, that international--customary  
8 international law, as it has now developed,  
9 prohibits some types of discrimination. There is  
10 no attempt by Professor Crawford to detail  
11 precisely what types of discrimination, but I think  
12 this does recognize that some discrimination is,  
13 indeed, a violation of 1105 under the customary  
14 international law rubric of it.

15 Does that answer your question?

16 ARBITRATOR REISMAN: I'm not sure, but I  
17 appreciate your response.

18 MR. DUGAN: Now, the other two principles  
19 that I think are articulated here are the complete  
20 lack of transparency and candor in an  
21 administrative process. And I think that that's

1 precisely what was violated here as well. I think  
2 that Governor Davis's shift is his ban on methanol  
3 and his unjustified shift--his ban on MTBE and his  
4 unjustified shift to ethanol were the result of a  
5 completely nontransparent process, that they were  
6 motivated by attempts to favor the interests of  
7 political contributors, that there was no candid  
8 disclosure of why the shift was being made,  
9 especially the shift to ethanol, the precipitous  
10 shift to ethanol, that these are the same types of  
11 government dealings that were called into question  
12 in Metalclad, for example, the one that required,  
13 that found the transparency was one of the most  
14 important or was an important objective of NAFTA,  
15 and I think that the same issues are in play here.

16           If, as we assert, what was going on behind  
17 the scenes was an attempt by Davis to favor one of  
18 the groups that had supported him, then that type  
19 of background undisclosed favoritism violates the  
20 principles of transparency and candor that  
21 Professor Crawford has identified here as being

1 part of the fair and equitable standard.

2           ARBITRATOR REISMAN: I would like to  
3 understand the quotation from waste management,  
4 since it is being presented now as in effect the  
5 only authority we have for the proposition that  
6 you're making.

7           MR. DUGAN: I'm sorry, for which  
8 proposition precisely?

9           ARBITRATOR REISMAN: The proposition that  
10 discrimination between an alien and a national is a  
11 violation of customary international law or at  
12 least 1105. I just want to go back, since we're  
13 looking at that, Professor Crawford lists all of  
14 those things and then says and exposes the claimant  
15 to sectional or racial prejudice, and that's  
16 cumulative. Does he mean--I'm asking you. I don't  
17 know. You're citing the case to us. Does that  
18 mean that he is suggesting that this list of  
19 horrors, arbitrary, grossly unfair and so on, must  
20 accumulate with the additional factor that it  
21 exposes the claimant to sectional or racial

1 prejudice, or do they stand alone?

2           MR. DUGAN: I think they stand alone, and  
3 I think that he didn't use a comma between  
4 "discriminatory" and "and," as is often the case,  
5 but I think there is a comma implied there, and I  
6 think each one of these is a separate heading, a  
7 separate principle. Take, for example, grossly  
8 unfair. I think to a degree that concept--that  
9 encompasses the concepts of natural justice, I mean  
10 of denial of justice, although I see that's also  
11 mentioned below, but I think if there were a  
12 showing that a particular situation, a particular  
13 outcome at hands of a government were grossly  
14 unfair, that that, in and of itself, would be  
15 enough to sustain a violation of the requirement of  
16 fair and equitable treatment, even if it didn't  
17 culminate in an episode of sectional or racial  
18 prejudice.

19           So, I think it is quite clearly from the  
20 way it's expressed a stand-alone principle, not  
21 tied to the last segment.

1           Now, one last point. This 1105 claim is  
2 independent of the 1102 claim. It doesn't require  
3 a showing of like circumstances, and it doesn't  
4 require a showing of disparate treatment. If under  
5 Professor Crawford's analysis Methanex can show  
6 that Davis's switch to ethanol was arbitrary and  
7 grossly unjust, there is no need to meet the  
8 requirements of Article 1102.

9           Now, with respect to Article 1110,  
10 Methanex does, indeed, have a very serious 1110  
11 claim. That was its original claim, and it's  
12 always maintained that claim. Methanex alleges  
13 that California expropriated Methanex's California  
14 market share, its customers in California, which  
15 substantially interferes with its ability to do  
16 business in California and interferes with its  
17 expectations of what it was going to be able to do  
18 in California. And I don't have it as a chart, but  
19 I would like read to you what I think is the test  
20 for an expropriation that was articulated in the  
21 Metalclad case. Expropriation of NAFTA includes

1 not only open, deliberate, and acknowledged takings  
2 of properties, such as outright seizure or formal  
3 or obligatory transfer of title in favor of the  
4 host state, but also covert or incidental  
5 interference with the use of property which has the  
6 effect of depriving the owner in whole or in  
7 significant part of the use or reasonably to be  
8 expected economic benefit of property, even if not  
9 necessarily to the obvious benefit of the host  
10 state. That's the Metalclad standard. And we  
11 think that's applicable here precisely, that what  
12 California did was it took Methanex's California  
13 market share, the sales that it had been making to  
14 the refiners such as Chevron, and Tosco and Valero,  
15 and it interfered with Methanex's ability to do  
16 business in that market, and it gave that market  
17 share to the U.S. ethanol industry, and that is a  
18 significant deprivation of Methanex's market share  
19 in the United States. It's a complete deprivation  
20 of Methanex's market in California, and that was  
21 not a reasonably to be expected outcome. Methanex

1 could not expect that California would  
2 precipitously and without any environmental  
3 justification shift to ethanol. And as a  
4 consequence, that seizure of its market in  
5 California and turning it over to the U.S. ethanol  
6 industry meets the criteria of an uncompensated and  
7 in fact illegal expropriation in California.

8           Now, I won't go over what we've already  
9 put in the record about market share, customer  
10 base, and goodwill being precisely the types of  
11 intangible property that's protected by Article  
12 1139 of NAFTA. We'll rest on the record with  
13 respect to that.

14           Now, I would like to turn now to the  
15 question of the intent to harm foreign methanol  
16 producers and how that intent should be inferred  
17 from the evidence in the record, the inferences  
18 that should be drawn.

19           Methanex believed that the test  
20 articulated by the Tribunal in the Partial Award is  
21 met here. The Tribunal can infer an intent to harm

1 based on two legal principles, two very well  
2 developed legal principles. The first is the  
3 principle of foreseeability. It's a well  
4 established principle of law that an actor intends  
5 the reasonably foreseeable consequences of his  
6 actions.

7           Second, where two entities compete  
8 directly for the same thing, in the same market, an  
9 intent to harm one is the same as an intent to harm  
10 the other. And because we believe we have  
11 shown--I'm sorry, if I mangled it, I think you  
12 understand what I'm saying, that an intent to  
13 benefit one is an intent to harm the other.

14           I think we've shown that Methanol competes  
15 directly with ethanol for the same market, the  
16 market being the use of oxygenates in the  
17 production of RFG in California. And if that's the  
18 case, if there is this direct competitive link,  
19 then any attempt to benefit one, by definition, by  
20 legal operation, harms the other. It has to,  
21 because there is no other consequence that can

1 result from that.

2           Now, turning to the first principle,  
3 foreseeability, as I said, I think it's a standard  
4 principle of law in all municipal systems and in  
5 international law as well, that intent to cause  
6 harm will be inferred where that harm is natural,  
7 probable, and the foreseeable consequence of taking  
8 a particular action.

9           We have a quote from Prosser and Keeton on  
10 torts that very concisely sums it up. Where the  
11 known danger ceases to be only a foreseeable risk  
12 and becomes in the mind of the actor a substantial  
13 certainty, the actor is presumed to cause the  
14 dangerous result. The restatement second of torts.

15           All consequences which the actor desires  
16 to bring about are intended as the word is used in  
17 this restatement. Intent is not, however, limited  
18 to consequences which are desired. If the actor  
19 knows that the consequences are certain or  
20 substantially certain to result from his act and  
21 still goes ahead, he is treated by the law as if he

1 had, in fact, desired to produce the result.

2           Now, in terms of the damage to Methanex,  
3 the question of whether the damage is foreseeable,  
4 I think, cannot be disputed. And we have included  
5 here a slide that the United States, from the  
6 United States's own EPA report in 1993, in which it  
7 not only recognized the harm to foreign methanol  
8 producers was foreseeable, it actually foresaw the  
9 harm that a set aside for ethanol would inflict on  
10 foreign methanol producers. Again, the primary  
11 impacts of this proposal include, and I'm skipping,  
12 the impacts on the various oxygenate and fuel  
13 industries affected. And it goes to say, and I'm  
14 selectively quoting here, the revenues and net  
15 incomes both corn farmers and ethanol producers  
16 should rise significantly due to higher corn and  
17 ethanol demand in prices, respectively. Revenues  
18 and net incomes of domestic methanol producers and  
19 overseas producers of both methanol and MTBE would  
20 likely decrease due to reduced demand in prices.

21           Now, again--

1           ARBITRATOR ROWLEY: Can you remind me of  
2 the date of this quotation.

3           MR. DUGAN: The date of that quotation is  
4 in 1993. But again, the mechanics--

5           ARBITRATOR ROWLEY: And can you help with  
6 the fact that it is five years before, or six or  
7 seven years before the measures in question?

8           MR. DUGAN: It was, indeed, before that,  
9 but I think that the fact it was before that is  
10 irrelevant because the market dynamics did not  
11 change, and it was foreseeable and, indeed,  
12 foreseen, that a shift of 30 percent of the market  
13 to ethanol would have a primary impact on foreign  
14 methanol producers. For the same reasons that the  
15 United States could foresee that shift in 1993, it  
16 was foreseeable in 1999 that the ban on MTBE and  
17 the precipitous shift to ethanol would have  
18 precisely the same easily foreseen impact on  
19 foreign methanol producers. It was foreseeable,  
20 and because it was foreseeable, it's entirely  
21 appropriate for the Tribunal to infer that it was

1 intended.

2           ARBITRATOR REISMAN: I just want to  
3 understand that. It seems rather sweeping to say  
4 that foreseeability in the determination of the  
5 aggregate consequences of the public policy are  
6 deemed to be intent. Under the interpretation that  
7 you're proposing, the last sentence of this  
8 excerpt, oil refiners could experience transition  
9 costs due to an intentional--additional  
10 requirement, also requires us to assume there was  
11 an intention to create higher transitional costs  
12 for oil refiners, which would also be actionable.

13           MR. DUGAN: I'm not sure it would be  
14 actionable, but if I could just--

15           ARBITRATOR REISMAN: But you would still  
16 say that this is deemed to be intent because the  
17 public policy analysis indicated the aggregate  
18 consequences.

19           MR. DUGAN: Well, I mean, I think you  
20 could restrict it to the particular facts of this  
21 case. The Tribunal has posited a very specific

1 test, a very specific intent to harm case under  
2 what it believe to be the facts of the case when it  
3 issued the Partial Award. As I said, we believe  
4 the facts are different, but I think you can  
5 confine it to the particular facts of this case.  
6 There is no general liability for acts which result  
7 in consequences that are foreseeable under either  
8 international law or U.S. regulatory law as far as  
9 I know.

10           The fact that a particular consequence can  
11 be understood as having been intended because it  
12 was foreseeable does not create a cause of action  
13 under U.S. law that I know of. But I think that  
14 for purposes of analyzing this case, where the  
15 Tribunal has said that inferences are, indeed,  
16 permissible, that this is a permissible inference,  
17 and, in fact, I think it's impossible to deny that  
18 this is a permissible inference when the common law  
19 is so clear that it is, indeed, a permissible  
20 inference, and because where the evidence I believe  
21 is so clear it was foreseeable and indeed foreseen

1 by the United States.

2 Now, in addition, the second piece of very  
3 important evidence about the foreseeability of the  
4 harm to Methanex, I think, is the statement by  
5 Senator John Burton. The two statements by Senator  
6 John Burton.

7 PRESIDENT VEEDER: Before you go to that,  
8 a silly point on the wording of this document.  
9 Rely upon this as formal admission, binding on the  
10 United States regardless of the evidence. That's  
11 your primary purpose in referring to this document.

12 MR. DUGAN: Well, reply at a minimum as  
13 extremely persuasive evidence, if not a binding  
14 admission.

15 PRESIDENT VEEDER: Just look at the last  
16 sentence. Revenues net incomes of domestic  
17 methanol producers and overseas producers of both  
18 methanol and MTBE would likely decrease.

19 Why are domestic producers of MTBE covered  
20 by that sentence? Why is that omitted?

21 MR. DUGAN: I don't know. I suspect it

1 was just an oversight by their part, and I don't  
2 think that omission in any material way affects  
3 their conclusion, the fact that they foresaw a  
4 shift to ethanol of 30 percent of the market would  
5 have a very damaging impact on foreign methanol  
6 producers.

7           And again, what happened in California, of  
8 course, was a hundred percent shift to ethanol, and  
9 if a 30 percent shift to ethanol would have a  
10 damaging impact, then it stands to reason that a  
11 hundred percent shift would have the same type of  
12 damaging impact.

13           Now, the second point, the second piece of  
14 evidence from which you can find foreseeability are  
15 the two comments Senator Burton made to the  
16 Methanex representatives, and the methanol  
17 representatives in the famous meeting where he told  
18 them that you're blanked and he said to sell  
19 Methanex stock short.

20           Professor, you raised the question, well,  
21 isn't that capable of two interpretations? Doesn't

1 that mean simply that you're going to lose? And in  
2 thinking about it, I think the appropriate response  
3 is that when it's phrased in that way, it means two  
4 things. It means you're going lose, and you're  
5 going to be harmed. Both of those meanings are  
6 contained within that statement. And, Mr. Veeder,  
7 you asked the question, but is he an actor? And we  
8 would agree that certainly with respect to the  
9 formal processes, he was not an actor.

10 But, his knowledge reflects two things.  
11 It reflects the foreseeability of harm to Methanex  
12 from the MTBE ban, and it reflects to a degree the  
13 knowledge of how the California government was  
14 going to act. It reflects to a degree the  
15 knowledge of how Governor Davis was going to act.  
16 I think you can infer from his statement that it  
17 was fairly common knowledge that Governor Davis was  
18 going to implement the ban against MTBE.

19 And again, if our submission that the date  
20 on which Mr. Vind had his conversation with Gray  
21 Davis about the compromise, can't you work out a

1 compromise so that the ethanol producers get some,  
2 and the refiners' concerns about supply are  
3 satisfied, that would have taken place a month  
4 before, which is further evidence that Governor  
5 Davis had already made up his mind and further  
6 evidence that knowledge about the ban is spreading.

7           So, we think from this it shows two  
8 things: Again, foreseeability and the state of  
9 Governor Davis's mind, that it was known that this  
10 was going to have a damaging impact on methanol  
11 producers, and foreign methanol producers, as well.

12           So, it is a good piece of evidence for  
13 foreseeability, and from foreseeability we argue  
14 that you can, and should, infer an intent to harm.

15           ARBITRATOR ROWLEY: If Governor Davis had  
16 been considering the MTBE issue, the UC report  
17 leading up to his election and, indeed, had been  
18 tending towards a decision or had even reached a  
19 decision that it would be, if elected, his  
20 recommendation would be that MTBE be banned and  
21 that ethanol be studied as a substitute all prior

1 to the dinner and receipt of donations from ADM,  
2 would that affect your case?

3 MR. DUGAN: If he had decided that all  
4 prior to the dinner?

5 ARBITRATOR ROWLEY: Yes.

6 MR. DUGAN: It would depend--

7 ARBITRATOR ROWLEY: I said prior to the  
8 dinner and/or receipt of the earlier donations.

9 MR. DUGAN: I understand.

10 Not necessarily. It would certainly make  
11 more difficult from an evidentiary point of view,  
12 but recall here that Davis sought out ADM and he  
13 sought out ADM, I think, and Mr. Vind testified  
14 because he wanted money from ADM.

15 Now, if he made the decision in  
16 anticipation of a rich stream of contributions from  
17 one of the largest contributors in the nation,  
18 then, no, it wouldn't affect our case. I think it  
19 would make the evidentiary inference to be drawn  
20 much harder, but it wouldn't affect the case. I  
21 think what's critical here is that the sequence of

1 events is that based on the evidence ADM had not  
2 made that decision. ADM certainly had not made  
3 that decision, and it made the decision after the  
4 meeting in Illinois, and we submit it made the  
5 decision based on something that happened at the  
6 meeting in Illinois. And what happened, again, we  
7 submit, was there was some type of implicit  
8 agreement that Governor Davis would expand the use  
9 of ethanol.

10           So, I think the only concern we would have  
11 under those facts is an evidentiary concern and not  
12 a theoretical concern.

13           Does that answer the question?

14           ARBITRATOR ROWLEY: It helps, thank you.

15           MR. DUGAN: All right. Now, turning to  
16 the second principle on which we think that it's  
17 appropriate for the Tribunal to infer a specific  
18 intent to harm, we've tried to show that--I think  
19 we have shown that this is a market where there is  
20 a binary choice, at least with respect to the  
21 integrated oil companies. Prior to the ban they

1 chose methanol. Now they choose ethanol in order  
2 to manufacture their RFG. And we think in those  
3 circumstances where there is a direct competitive  
4 link, where it's a zero-sum game, where the  
5 competitor gets the whole pot or none of it, that  
6 that competitive link alters the types of  
7 inferences that can be drawn.

8           Now we think that almost--that most, and  
9 perhaps all antidiscrimination regimes recognize  
10 that an intent to favor one competitor demonstrates  
11 by definition at a harm and intent to harm the  
12 disfavored competitors. And it appears--it's almost  
13 self-evident, if do you have a pot of--a zero-sum  
14 game where someone is favored, then someone by  
15 definition is going to be disfavored, and intent to  
16 favor the one has to be construed as an intent to  
17 favor the other.

18           And I think the U.S. itself recognized  
19 that in their statement on July 12, 2001, which is  
20 Tab 31. Just quoting the highlighted sections, why  
21 would California have any interest in injuring

1 foreign owned producers if not to benefit U.S.  
2 domestic ethanol industry, quoting selectively  
3 there? And I think that's the gist of it. As the  
4 U.S. itself at least implicitly recognized, these  
5 are two sides of the same coin.

6           Now, again, this principle, it's not a  
7 novel principle. Methanex is not putting it  
8 forward in the absence of very considerable legal  
9 support. If you turn to Tab 32, the statement has  
10 been--this is from the WTO decision: If there is  
11 less favorable treatment of the group of like  
12 imported products, there is, conversely, protection  
13 of the group of like domestic products.

14           Professor--and I think one particularly  
15 good articulation of the theory is found in the  
16 Bacchus Imports, Limited, case. That was a United  
17 States Supreme Court case dealing with what's known  
18 as the dormant commerce clause, which is a  
19 prohibition on the type of economic protectionism  
20 that we are talking about. It's internal to the  
21 United States. It's not a rule of international

1 law, but the analog is very, very close to what's  
2 being dealt with here.

3           That case involved a tax law that the  
4 State of Hawaii had passed which exempted two  
5 locally produced liquors from a general Hawaii tax,  
6 but the tax was applied to all other beverages  
7 originating in state or out of state. Hawaii  
8 argued that it didn't intend to discriminate  
9 against products from out of state. It merely  
10 intended to favor a couple of domestic products,  
11 and urging that there was no discriminatory intent  
12 on the part of the state legislature because the  
13 exemptions in question were not enacted to  
14 discriminate against foreign products, but rather  
15 to promote a local industry.

16           The Supreme Court rejected that, and they  
17 rejected that using language that I think is very,  
18 very relevant here: Virtually every discriminatory  
19 statute allocates benefits or burdens unequally.  
20 Each can be viewed as conferring a benefit on one  
21 party and a detriment on the other in either an

1 absolute or relative sense. The determination of  
2 the constitutionality does not depend upon whether  
3 one focuses on the benefited or the burdened party.  
4 A discrimination claim by its nature requires a  
5 comparison of the two classifications, and it could  
6 always be said that there was no intent to impose a  
7 burden on one party, but rather the intent to  
8 confer a benefit on the other.

9           Consequently, it is irrelevant to the  
10 commerce clause inquiry that the motivation of the  
11 legislature was the desire to aid the makers of the  
12 locally produced beverage rather than to harm  
13 out-of-state producers.

14           Now, again, we think that there is ample  
15 legal precedent for this type of inference drawing,  
16 and we believe that the United States has itself  
17 adopted this type of inference drawing in the  
18 positions it's taken in trade cases. This was  
19 the--actually, this was the position taken by the  
20 United States in the Japan measures affecting  
21 consumer photographic film and paper. Regardless

1 of whether Japan has sought to hinder imports or  
2 merely help domestic producers, the direct  
3 consequences of its actions were to diminish  
4 opportunities for foreign photographic material  
5 manufacturers and to distribute their products. By  
6 creating distribution channels open exclusively to  
7 domestic manufacturers, Japan intentionally  
8 enhanced competitive opportunities for domestic  
9 manufacturers to the detriment of imports.

10           Again, two sides to the same coin.

11           And that's precisely the case here. You  
12 have a binary market where in 1999, methanol  
13 completely dominated the market for oxygenates used  
14 by integrated oil companies in the production of  
15 RFG. Now, it has no market share of that  
16 whatsoever. That has all shifted to ethanol, and  
17 it shifted to ethanol because of Davis's actions in  
18 precipitously selecting ethanol as the favored  
19 replacement.

20           Now, that's a zero-sum game. Integrated  
21 oil companies have to buy oxygenates in order to

1 comply with the requirement to produce RFG, and by  
2 intending to favor domestic ethanol industry,  
3 Governor Davis, by definition, intended to harm all  
4 its foreign producers because the two are opposite  
5 sides of the same coin. And it's because of the  
6 competitive relationship, the direct competitive  
7 relationship between the two products.

8           Next, I would like to turn to the question  
9 of Methanex's ownership of investments in the  
10 United States, and--

11           PRESIDENT VEEDER: Just before do you  
12 that, we are not pressing you, but can you give us  
13 some rough estimate of how far you've got, and how  
14 much further time you need.

15           MR. DUGAN: I suspect I'll need about an  
16 hour and 15 minutes.

17           PRESIDENT VEEDER: That will take us up  
18 7:00.

19           MR. DUGAN: About that, yes.

20           PRESIDENT VEEDER: It's when you rest that  
21 we go beyond seven because that, for administrative

1969

1 reasons, very much the last time we can sit without  
2 making special arrangements.

3 MR. DUGAN: No. I will certainly do my  
4 best. I think I can get it done by seven. I will  
5 certainly try.

6 PRESIDENT VEEDER: We're not pressing you.  
7 You must take the time you need, but if you need  
8 longer, I think you need to tell us. Seven o'clock  
9 is still okay.

10 MR. DUGAN: I don't think I will need  
11 longer.

12 PRESIDENT VEEDER: Let's work on that  
13 basis. We'll need another short break I think just  
14 to give the stenographer a little rest.

15 MR. DUGAN: Now is as good a time as any,  
16 if you want to do it now or we can do it later.

17 PRESIDENT VEEDER: Let's do it now.

18 MR. DUGAN: Okay.

19 (Brief recess.)

20 PRESIDENT VEEDER: Let's resume.

21 Before we do so, could we review

1970

1 administrative arrangements for tomorrow. On one  
2 view, in the light of today, we should start  
3 earlier. On another view, because it may be that  
4 time has been removed from the United States in  
5 preparing for tomorrow, we should start later. We  
6 should ask the United States as to what their  
7 preference would be. It has to be one or the  
8 other.

9 MR. LEGUM: It's the latter of the two.  
10 We would prefer to start a bit later, around 2:30  
11 is what we are proposing.

12 PRESIDENT VEEDER: If we did that, we  
13 would have to be pretty sure of finishing before  
14 7:00. Is that still your intention?

15 MR. LEGUM: It is, indeed.

16 PRESIDENT VEEDER: And we ought to allow  
17 quarter an hour at the end for various housekeeping  
18 matters so that would probably mean 6:45. Does  
19 that make a difference to your answer?

20 MR. LEGUM: No, no, it doesn't.

21 PRESIDENT VEEDER: So, 2:30 tomorrow. We

1 will continue until 7:00.

2 Does that cause any difficulties, Mr.

3 Dugan?

4 MR. DUGAN: No, that's fine.

5 PRESIDENT VEEDER: Mr. Dugan, let's go on.

6 MR. DUGAN: Okay. Thank you.

7 Next, I would like to turn to the question  
8 of Methanex's ownership of investments in the  
9 United States. The U.S. asserts that Methanex has  
10 not shown that it actually owns any U.S.  
11 investments. Now, Methanex--from Methanex's point  
12 of view, this is an entirely frivolous argument,  
13 and the Tribunal shouldn't be wasting any time on  
14 it, and neither should the parties.

15 The U.S. asserts, quote, the United  
16 States, as a respondent in this billion dollar  
17 case, has the right to insist on evidence of  
18 ownership as authoritative as what would be  
19 required in a corporate transaction.

20 Now, the U.S.--

21 PRESIDENT VEEDER: You're quoting from

1 what?

2 MR. DUGAN: I'm quoting from transcript  
3 page 577, lines 6 to 11.

4 The United States cites absolutely no  
5 authority whatsoever for the fact that they're  
6 entitled to a certain level of evidence with  
7 respect to a particular point that's in dispute.  
8 And actually it's not even in dispute. And we  
9 submit that they're not. They're simply making  
10 that up. They're not entitled to evidence as  
11 authoritative as if included in a corporate  
12 transaction, and there is not a shred of authority  
13 to support that.

14 What's on the record here is that Methanex  
15 has provided ample, credible, uncontradicted  
16 evidence of its ownership, and that's an end to it.

17 Let's go to Mr. Macdonald's witness  
18 statement. This is what he said: Methanex owns  
19 several companies in the United States. Of these,  
20 there are two principal operating entities:  
21 Methanex Methanol Company, Methanex-US, which is

1 responsible for methanol sales and inventory; and  
2 Methanex-Fortier, Inc., which is responsible for  
3 methanol production. Methanex-US is a Texas  
4 general partnership owned by two companies,  
5 Methanex, Inc., and Methanex Gulf Coast, Inc., both  
6 incorporated in the State of Delaware. Methanex  
7 indirectly owns 100 percent of the shares of both  
8 partners. Methanex-Fortier is also incorporated in  
9 Delaware, and Methanex also indirectly owns  
10 100 percent of the shares in this company. While  
11 the U.S. apparently is part of a scorched-earth  
12 litigation approach questions these facts, I'm  
13 pleased to assure the Tribunal of the very real and  
14 legal existence. In fact, I'm a director and vice  
15 president of each of these companies.

16           So, there you have sworn testimony from a  
17 director and officer of the companies as to the  
18 ownership that's there.

19           Now, the U.S.--and he further provided a  
20 detailed chart that specifically corroborates these  
21 statements. We submit that there is actually no

1 basis to challenge them. They didn't even bother  
2 to cross-examine Mr. Macdonald. This is  
3 uncontroverted, clearly competent evidence as to  
4 who owns these companies, and that should be an end  
5 to it.

6           Now, even beyond that, they say there is  
7 no additional evidence of that. If you see at the  
8 next page, this is a chart from Methanex's annual  
9 report. It's a simplified chart, but it shows the  
10 same thing.

11           Now, again, this was filed with the United  
12 States Securities and Exchange Commission under  
13 penalty, criminal penalties, if it's fraudulent or  
14 wrong. The U.S. ignored this completely, and  
15 insisted time and time again that Mr. Macdonald  
16 produced more and more evidence of the evidence of  
17 ownership.

18           And finally, the United States has not  
19 asserted any reason to disbelieve anything that  
20 Mr. Macdonald has said. It has done nothing. It's  
21 provided no evidence to rebut anything that

1 Mr. Macdonald has said. This is sheer vexatious  
2 litigation with no basis in the record whatever.

3 Now, that said, this is a good time to  
4 talk about costs. Methanex believes it's fully  
5 entitled to all costs and fees in this case because  
6 of this type of vexatious litigation tactic. The  
7 no-investment argument was frivolous. It never  
8 should have been brought, and it should have never  
9 been pursued. And the same was true at the  
10 jurisdictional stage. If you recall, the United  
11 States, I think, launched a number of  
12 jurisdictional challenges, either six or seven, and  
13 lost most of them. And the reason it lost most of  
14 them is it didn't belong at that stage. I never  
15 heard of a proximate cause challenge to the  
16 jurisdictional phase, and on its face it seems to  
17 be frivolous. Proximate cause analysis is so  
18 entirely bound up with the facts of the case that  
19 bringing it at that stage can only be considered as  
20 vexatious and frivolous.

21 Now, just because this is unusual case

1 with unusual allegations under a novel legal  
2 instrument that's only been around for 10 years in  
3 an area of law that's developing, that doesn't  
4 justify putting up frivolous argument after  
5 frivolous argument, and we think that's has been  
6 the case here. And we think because of the way the  
7 United States has conducted this litigation it  
8 should be liable for all the costs and fees.

9           Next, I would like to go to the question  
10 of damages, and the first point I would like to  
11 make--and I don't think this is rebutted by the  
12 United States--the most obvious element of damages  
13 here is that Methanex has now lost its California  
14 market. It's lost its customers in California.  
15 Prior to the time of the ban, it used to sell to  
16 Chevron and Valero and Tosco and the other  
17 integrated oil companies, all of which are set  
18 forth in the record. Now it cannot sell to them.  
19 That loss of revenue, that loss of customers, that  
20 loss of market share is an obvious damage to the  
21 corporation, and United States does nothing really

1 to refute that.

2           Secondly is the drop in the share price,  
3 and the United States says that Methanex keeps  
4 coming up with different theories, and Methanex, in  
5 response to United States, went back and looked at  
6 the one period that the United States had  
7 proffered, which was in late January, early  
8 February, 1999, to see what was the cause of that  
9 decline. And it turns out from the record, which  
10 is copiously described by Mr. Macdonald in his  
11 affidavit, that drop was caused by the MTBE ban, as  
12 well.

13           So, in terms of damage to the corporation  
14 reflected by the stock price, we, in essence, break  
15 it up into three segments: We have the preemptive  
16 drop of approximately 21 percent in late January  
17 and early February--and again, the evidence is in  
18 the record that the MTBE ban was very much on the  
19 minds of investors at that time--we had the  
20 immediate drop of 10 percent on the day after the  
21 ban was announced; and we have the same drop of

1 15 percent over the next 10 days. And the total of  
2 those cumulate to approximately 30 percent.

3           And that is a fact which shows very, very  
4 severe damage to Methanex as a corporation. And  
5 there is no showing--you will see at the right-hand  
6 side of that that the price has since climbed back  
7 up. That's because of the price of methanol has  
8 gone up. But there has been no showing that the  
9 damage that was inflicted upon Methanex by the MTBE  
10 ban has been fully recovered. The United States  
11 simply hasn't shown it.

12           And a generalized showing that the share  
13 price has increased is not a particularized showing  
14 that there has not been a fact of damage. That, I  
15 think, is conclusively established by the drop in  
16 the share price that we tied to analyst reports and  
17 we tied to the timing of the MTBE ban.

18           Now, the U.S. also asserts that a drop in  
19 share price is not a damage to a corporation. It's  
20 a damage to the corporation shareholders. And as a  
21 matter of law, we think that that's just not true.

1 I'm skipping over a couple of exhibits that show  
2 fairly graphically the drop in the share price, but  
3 if I could get to the legal issues--and this is Tab  
4 40--these are some quotes from some authoritative  
5 sources.

6 Diminution--

7 MR. LEGUM: Mr. President, these are  
8 authorities that have never been before offered to  
9 the Tribunal or to the United States, and we object  
10 to their being introduced at such a late date.

11 PRESIDENT VEEDER: Are all these new, Mr.  
12 Dugan?

13 MR. DUGAN: They are new, but I didn't--I  
14 had no idea that I didn't understand that the  
15 closing argument was limited to legal sources in  
16 direct. This is not evidence. This is law. And  
17 it's always been my understanding that you can put  
18 in new law at any stage up to the closing.

19 PRESIDENT VEEDER: Could we just raise a  
20 preliminary issue we would like to discuss with  
21 you, which is that we ordered bifurcation, and we

1 decided in our order last summer to put off all  
2 issues of quantum. Does that affect your argument?

3 MR. DUGAN: Well, if the Tribunal is  
4 willing to rule there is, in fact, damage, what the  
5 United States--the position that the United States  
6 is taking is that there is no damage whatsoever  
7 and, therefore, the case can't proceed. We agree  
8 with you completely that quantum has been put off,  
9 but we are trying to respond to the U.S. argument  
10 there has been no damage at all.

11 PRESIDENT VEEDER: So, you have got to  
12 establish the probability on the balance of  
13 probabilities. It's all or nothing.

14 MR. DUGAN: Exactly.

15 PRESIDENT VEEDER: And that gets you  
16 through the bifurcation.

17 MR. DUGAN: Correct, which gets us to the  
18 next stage. We are just trying to show that from  
19 the evidence in the record that the only thing the  
20 Tribunal can conclude is that there was, in fact,  
21 damage to the corporation. How much we have not

1 attempted to show.

2           PRESIDENT VEEDER: Before we look at this  
3 to make a ruling, could you talk us through the new  
4 legal materials. We are looking at Tab 40.

5           MR. DUGAN: This is Tab 40. These are  
6 things like the encyclopedia of private law of  
7 corporations that show, as a matter of law, a  
8 damage--a drop in the share price is a damage to  
9 the corporation.

10          PRESIDENT VEEDER: These are all U.S.  
11 legal tomorrows?

12          MR. DUGAN: These are all U.S. legal  
13 materials, yes.

14          PRESIDENT VEEDER: Just looking at these  
15 abstracts, and in the absence of some injury  
16 suffered by the corporation, can the corporation  
17 recover for a diminution in its share price?

18          MR. DUGAN: I think it depends on the  
19 circumstances. We're involved in a proceeding  
20 where we hope to recover not for the damage--not  
21 for the decrease in the share prices. We are

1 offering this--our calculation of damages is not  
2 based on the decrease in the share price. The  
3 calculation is based on an entirely different  
4 market analysis.

5           We proffer this as evidence of the fact  
6 that the drop in the share price is both a legal  
7 injury to the corporation and that it's evidence of  
8 the injury that the corporation suffered because of  
9 the MTBE ban.

10           And again, this is evidence that under  
11 some legal analysis, a drop in the share price is  
12 considered to be a direct injury to the  
13 corporation, and an injury which the shareholders  
14 can recover from for derivatively.

15           PRESIDENT VEEDER: Mr. Legum, I don't  
16 recall if we ever actually addressed whether new  
17 legal materials can be brought in at this stage.

18           MR. LEGUM: I don't believe there has been  
19 a specific ruling on that, either.

20           PRESIDENT VEEDER: Are there any other  
21 legal materials tonight that you are going to

1 introduce tonight that are new, Mr. Dugan?

2 MR. DUGAN: There is one source on  
3 proximate cause to Prosser and Keeton.

4 PRESIDENT VEEDER: What tab number is  
5 that?

6 MR. DUGAN: That would be Tab 52.

7 MR. LEGUM: I believe Tab 41 also reflects  
8 the new materials.

9 MR. DUGAN: Tab 41 as well, but that's the  
10 same thing we're arguing about right here. But the  
11 Prosser and Keeton description of proximate cause,  
12 I think, has been included in the legal materials  
13 before this. It's--certainly the basic  
14 description, I think, has been included.

15 PRESIDENT VEEDER: Mr. Legum, given we may  
16 take some time to debate this, we are minded it to  
17 let it in. If it causes a difficulty to the United  
18 States in presenting this tomorrow, we will  
19 obviously hear you sympathetically tomorrow.

20 MR. LEGUM: Very well, but in the  
21 meantime, I'm assuming that Methanex will be

1 providing us and the Tribunal with fuller copies of  
2 these authorities?

3 PRESIDENT VEEDER: Well, this is the  
4 difficulty. I think these are sound bites and they  
5 don't go very far as bound bites, particularly  
6 since they are limited to U.S. legal materials.

7 Were you intending to put in the full  
8 report, Mr. Dugan?

9 MR. DUGAN: We could certainly put in the  
10 full report.

11 PRESIDENT VEEDER: We're not necessarily  
12 asking for you to do that, but I'm asking whether  
13 you intend to do that.

14 MR. DUGAN: We'll do that. We'll provide  
15 them--

16 PRESIDENT VEEDER: And can you get those  
17 to the United States tonight?

18 MR. DUGAN: We could get them to the  
19 United States tonight, yes.

20 PRESIDENT VEEDER: I think they are more  
21 important than us tonight. They've got to have a

1 chance to consider these new materials.

2           And again, if the United States has any  
3 new legal materials tomorrow, it's useful to get  
4 them over to Mr. Dugan before we start at least at  
5 2:30.

6           MR. LEGUM: I don't think we will, but if  
7 we do, we will.

8           MR. DUGAN: All right. I won't read each  
9 one of these individually. The first one, I think,  
10 states the principle very concisely. Diminution in  
11 the value of corporate stock resulting from some  
12 depreciation or injury to corporate assets is a  
13 direct injury only to the corporation. It is  
14 merely indirect or incidental injury to an  
15 individual shareholder.

16           And we submit that, applied here, that  
17 principle shows that the diminution in the value of  
18 Methanex's stock resulting from the MTBE ban which  
19 eliminated its market in California is a direct  
20 injury to the corporation, and that that--applying  
21 that principle to the facts of the Methanex share

1 drop conclusively establishes the fact of damage to  
2 Methanex.

3           Now, whether or not that damage has been  
4 mitigated by the rise in the share prices as a  
5 result of the change in the price of methanol, is  
6 no way a showing that that damage has been  
7 alleviated; and the fact of the matter is, it  
8 hasn't. And that fact of damage is enough to  
9 establish the level of damage needed to get through  
10 to the second phase, the bifurcated phase, of the  
11 hearing.

12           Now, the U.S. also argues that the drop in  
13 the debt rating that Methanex quite clearly  
14 suffered is not damaged because Methanex didn't  
15 issue any debt, which is true. But again, Methanex  
16 would submit that whenever a corporation has to  
17 suffer a public downgrading of its debt rating, and  
18 when that downgrading is expressly tied to an MTBE  
19 ban, that alone is a fact of damage. The quantum  
20 of that damage may be very difficult to quantify,  
21 but a decrease in the debt rating, if nothing else,

1 causes reputational harm. It undoubtedly has a  
2 carryover to the damage inflicted on the share  
3 price, but that alone is a fact of damage that's  
4 sufficient to establish damage for purposes of  
5 1116.

6           Next, the U.S. does not dispute that the  
7 shift to ethanol in California has resulted in a  
8 permanent loss of 6 percent of world demand. The  
9 statements of Pierre Choquette that they cited  
10 illustrate that. And if you will turn to Tab 42,  
11 Mr. Choquette talks about the reduction in MTBE  
12 consumption in the United States is taking place,  
13 but, of course, it's overshadowed by supply  
14 constraints, so it's hard to see the impact of the  
15 reduction.

16           First of all, he doesn't say it doesn't  
17 cause any problems. He said it's overshadowed by  
18 supply constraints. But, more importantly, he  
19 talks about a loss of demand of 750,000 tons per  
20 year, and that's 50 percent of the market in 2002.  
21 If you double that, it's 1.5 million tons per year

1 in permanent demand loss. That's the impact of the  
2 ban in California on the global supply market.

3 Now, there is no doubt that methanol is a  
4 global commodity, and the price responds to those  
5 types of things quite quickly. And what we have  
6 cited next at Tab 43 is testimony from Mr. Burke:

7 Well, methanol is a globally traded  
8 commodity; do you agree with statement?

9 Yes, I would.

10 So, demand changes in one region  
11 ultimately affect the global supply and  
12 demand balance for methanol; you would  
13 agree with that?

14 Yes.

15 It's a global commodity, and any commodity  
16 market which use loses 6 percent of demand has lost  
17 a very significant element of demand.

18 Now, the next chart which is taken from a  
19 Methanex annual report, I think, illustrates this.  
20 You see this is the price history for methanol, and  
21 you can see that it's very, very volatile. It's

1 always been like that. Like many commodities, it's  
2 volatile. It could go up and down sharply.

3 Now, at the present time we're in a strong  
4 market, but the fact of the matter is with  
5 6 percent extra demand, the only inference the  
6 Tribunal can draw is that the price would be much  
7 higher. That's what happens: Supply and demand.

8 And you will see that the price of  
9 methanol went much higher in 1994, and Methanex  
10 submits that but for the 6 percent drop in demand  
11 caused by the shift to ethanol in California that  
12 the price of methanol would be approaching what it  
13 was in 1994. Methanex would be making more  
14 revenues and a lot more profits because the price  
15 would be higher.

16 Now, to get to some of Mr. Choquette's  
17 statements that we believe the United States took  
18 out of context, this is one of the statements that  
19 they quoted, and the full statement says this:  
20 There is no new news related to MTBE. It--the loss  
21 of the California market--just happens to be coming

1 at a time where it's unlikely to have any  
2 significant impact.

3 Now, that's the part they quoted. But he  
4 went on to say, The impact of what might happen in  
5 California over the next year, but, you know, the  
6 longer term, that the California MTBE ban would be  
7 a factor. Now, that's Mr. Choquette saying the  
8 long-term effect of the California ban is going to  
9 be a factor.

10 United States attributed almost prophetic  
11 status to everything Mr. Choquette says. Methanex  
12 submits that here he recognizes that in the long  
13 term it's going to be a factor, and quite obviously  
14 it's not going to be a good factor; it's going to  
15 be a damaging factor.

16 Similarly, next slide, page 46, the United  
17 States quoted the portion of the--this quote that's  
18 not highlighted, or it's not bolded: We don't  
19 expect the impact of such a change to have much of  
20 an impact on pricing, if at all. But, if you take  
21 the whole statement in context, he's obviously

1 talking about a short-term analysis. And again,  
2 many of these comments are made at either quarterly  
3 earnings conference calls or investor--investor  
4 meetings where the emphasis is almost always on the  
5 short term: As we look forward to the switch to  
6 ethanol over the next year or so--so, by the end  
7 this year, sometime early next year--in our view,  
8 the current supply-and-demand environment, and it  
9 goes on to quote the statement. This is very much  
10 a short-term analysis, not a long-term analysis.  
11 And in the long term, Mr. Choquette expressly  
12 recognized that there would be damage to Methanex.

13           Again, there was a selective quotation  
14 from Mr. Macdonald's affidavit. If you read the  
15 full quotation, he focuses--the last sentence: In  
16 other words, pricing is currently robust due to  
17 supply limitations compared to the underlying  
18 demand. That emphasis is supplied, but I think it  
19 illustrates the point. You can't extrapolate from  
20 what's happening right now in the market what's  
21 going to happen in the future. Methanol is very

1 volatile. The bottom could fall out of the market  
2 next month; and in that case, there could be  
3 buckets of red ink at Methanex, and the red ink  
4 will be even greater, the losses would be even  
5 greater, because at this point the methanol market  
6 has lost 6 percent of demand. And in a commodity  
7 market, and in global commodity market, that is a  
8 huge drop in demand that at the margins has a  
9 tremendous impact on the price, it has tremendous  
10 impacts on the revenues of Methanex, and it has a  
11 tremendous impacts on the profits of Methanex.

12           Now, with respect to Fortier, the next  
13 exhibit is the statement issued by--or I guess the  
14 annual report issued by Methanex at the time that  
15 it idled Fortier, and Fortier was not shut down in  
16 1999, and this says exactly what happened to it.  
17 In Fortier, Louisiana, we reached a new  
18 understanding with our partner, Cytec. As a  
19 result, we now have hundred percent ownership and  
20 gained much needed flexibility. This plant will  
21 remain shut down until market conditions are more

1 favorable. So, that's why it was idled, because it  
2 was waiting for better market conditions.

3           Now, again, the next slide is from  
4 Methanex's 2002 annual report, which the United  
5 States notes is filed with the SEC, subject to the  
6 stringent requirements of accurate reporting  
7 imposed by the securities laws. Limiting or  
8 eliminating the use of MTBE in gasoline in  
9 California or more broadly in the United States  
10 will reduce demand for MTBE and methanol in the  
11 United States and negatively impact the viability  
12 of MTBE and methanol plants such as our Fortier  
13 facility in the United States.

14           So, that's a securities law  
15 acknowledgement of the continuing impact of the  
16 MTBE ban on the viability of Fortier.

17           Now, what we have next in the book are two  
18 selections from Mr. Macdonald's third affidavit,  
19 and they're put in here just to show that all the  
20 while that Fortier was shut down, it was still  
21 being carried as a potentially--as a plant that

1 could potentially be reactivated if the price went  
2 up. And this is paragraph 10 of Macdonald's third  
3 affidavit: We have spent approximately 5 million  
4 cash per year over the past several years since  
5 idling the plant to maintain our ability and  
6 flexibility to reopen the plant. And while it  
7 would be accurate to say that a significant portion  
8 of this expenditure was to meet contractual  
9 obligations, it's also a fact that the structure of  
10 such payments was specifically tailored to maintain  
11 our ability to restart the plant.

12           Similarly, on the next page, Mr. Macdonald  
13 puts in testimony--and again, this testimony is  
14 uncross-examined and uncontradicted. It's one  
15 thing for the United States to speculate on what  
16 might have happened when Methanex did a particular  
17 act. It's another thing to try to bring out  
18 through cross-examination. They chose not to do  
19 that. And so this stands effectively unrebutted  
20 and uncontradicted.

21           Paragraph 12, Mr. Macdonald puts in

1 evidence as to why Fortier was finally and  
2 permanently shut down. On February 18, 2004, at a  
3 regular meeting of our executive leadership team,  
4 of which I'm a member, Methanex took the decision  
5 to cease all discretionary payments related to our  
6 Fortier and Medicine Hat, Canada plants and to  
7 proceed toward permanent abandonment of those  
8 assets. In arriving at this decision, our  
9 discussion included both aspects of the economic  
10 outlook for our remaining North American assets,  
11 namely gas price and market demand. The permanent  
12 loss of California MTBE demand with the ban now  
13 having been fully implemented and the losses  
14 triggered by bans in other states was a substantial  
15 consideration in our decision.

16           Again, Mr. Macdonald's testimony is  
17 uncontradicted, uncross-examined, and it has to be  
18 accepted as evidence of why Methanex finally  
19 decided to permanently close Fortier.

20           And I think if you put this together with  
21 the evidence about the 6 percent loss in demand and

1 the volatility of the market, the reason is quite  
2 clear. But for the California ban, there would be  
3 6 percent more demand. With 6 percent more demand,  
4 the price for methanol would be much higher. If  
5 the price for methanol was much higher, they  
6 wouldn't have decided to close Fortier.

7 So, it's Methanex's position that the ban  
8 in California had a direct link to the final  
9 closure of Methanex-Fortier.

10 Now, if the United States has said no, the  
11 reason why Methanex-Fortier was closed is because  
12 plants in the Gulf cannot make money because the  
13 price of gas is so high, and they're half right.  
14 The price of gas is very high, but that doesn't  
15 mean plants there can't make money. Plants make  
16 money if their price exceeds their costs, if their  
17 revenues exceed their costs.

18 And one of the pieces of evidence that the  
19 United States pointed to in showing how dire the  
20 situation is for the methanol industry of the  
21 United States was the statement of Mike Bennett.

1 It's at Tab 51. And it says that 34 percent of  
2 U.S. capacity has been permanently closed, which is  
3 true, but the converse of that is also true:  
4 66 percent of permanent capacity remains open--most  
5 of that is in the Gulf states--and there is no  
6 reason to believe they aren't making money;  
7 otherwise, they would be closed, too. And again,  
8 if the price were high enough, Fortier could have  
9 made money, regardless of the high cost of gas.  
10 And the price is not higher because of the  
11 6 percent drop in demand caused by the California  
12 MTBE ban.

13           The JS cite for that particular exhibit is  
14 16 JS tab 48. That's the Mike Bennett quote.

15           Now, Methanex believes that all five of  
16 those indicia of damage are sufficient to establish  
17 a very serious damage to the corporation. And  
18 again, the chart that the United States showed you  
19 showed an increase in share price and decrease in  
20 methanol price in recent years. There hasn't been  
21 any showing that that wiped out the damage. We

1 know that we have very significant damage in 1999  
2 when the price dropped--the price of the stock  
3 dropped precipitously, and we know that the debt  
4 rating dropped precipitously, or dropped. The U.S.  
5 cannot show that that damage was eliminated. A  
6 cyclical rise in the price of methanol does not  
7 necessarily eliminate all the damage that was  
8 inflicted at that time.

9           Now, would our damage calculation now be  
10 different from what it was in 1999? Almost  
11 certainly, but what that difference is, we don't  
12 know. It remains the fact that Methanex was  
13 damaged in 1999-2000, and remains damaged, and  
14 that's enough to satisfy the criteria at this stage  
15 and see the case through to the quantum stage with  
16 respect to damages.

17           Now, with respect to proximate cause, the  
18 chart we put up is just a plain vanilla  
19 description, a legal description of what is  
20 proximate cause from Prosser and Keeton, a  
21 well-known treatise in the United States. It's

1999

1 described--proximate causation is described as some  
2 reasonable connection between the act or omission  
3 of the defendant and the damage the plaintiff has  
4 suffered.

5           Now, two principal points with respect to  
6 this. Again, going back to the California market,  
7 it's a binary choice market. And I won't put the  
8 slide back up there, but from the slide that we put  
9 up previously, it shows it quite clearly. In 1999  
10 and 2000, Methanex and the methanol industry sold a  
11 lot of methanol into California. Now it sells  
12 none. 1999, Methanex had customers in California.  
13 The integrated oil refineries who bought methanol  
14 for use in making RFG. Now it has none.

15           And we showed you the Valero contract, and  
16 directly as a result of the California MTBE ban,  
17 Valero stopped buying methanol from Methanex.  
18 That, we contend, far more than meets the  
19 requirement of some reasonable connection between  
20 the act of the defendant and the damage the  
21 plaintiff has suffered. It's not just a reasonable

1 connection. It is direct cause and effect. The  
2 ban went in place, our customers disappeared. We  
3 submit that that satisfies any criteria for  
4 proximate cause.

5 In addition, we submit that the permanent  
6 drop of 6 percent demand and the admission by the  
7 United States expert that this is a global  
8 commodity market, that the ordinary understanding  
9 of any global commodity market is that when you  
10 have a 6 percent permanent drop in demand, that's  
11 going to permanently affect the price, at least  
12 until as long as the capacity is taken up. But  
13 that type of permanent drop in demand will have a  
14 corresponding impact--in fact an exaggerated  
15 impact--because it is a volatile commodity market  
16 that will continue to cause damage to Methanex for  
17 some period of time.

18 ARBITRATOR REISMAN: One clarification  
19 going back to Fortier. Fortier did not supply  
20 California; is that correct?

21 MR. DUGAN: Fortier did not supply

1 California, that's correct.

2 ARBITRATOR REISMAN: So, why would the  
3 drop in demand in California affect Fortier? I can  
4 understand why it would affect Medicine Hat, but  
5 why Fortier?

6 MR. DUGAN: Because it's a global market.

7 ARBITRATOR REISMAN: No, global market is  
8 simply a concept, but if Fortier does not sell  
9 under these circumstances to California--Fortier  
10 has a segmented customer base; it doesn't sell to  
11 California. Why is it that when California no  
12 longer purchases MTBE or allows MTBE Fortier  
13 suffers, what is the proximate relationship there?

14 MR. DUGAN: Perhaps you reject the notion  
15 of a global market, but when there is a decrease in  
16 demand, the plants that don't get reopened are the  
17 ones that operate at the margins. And again, had  
18 the price but for the California ban, the demand  
19 for MTBE would be higher. If the demand for MTBE  
20 were higher, the price would be higher. And if the  
21 price would be higher, Fortier could perhaps

1   reopen. That is the logical consequence. And it  
2   it's because it is a global market. It is a  
3   pricing factor because the MTBE ban has had such an  
4   impact on the price of methanol and depressed it  
5   below what it otherwise would be. That's what's  
6   contributed to the closure of Fortier.

7           Just so you don't misunderstand, the sales  
8   into California were sales from Methanex-US, the  
9   other main Methanex company.

10           ARBITRATOR REISMAN: Which is a marketing  
11   company?

12           MR. DUGAN: Which is a marketing and  
13   distribution company, which has real assets. It  
14   has a fleet of rail cars. It has leases where it  
15   stores it.

16           ARBITRATOR REISMAN: I'm glad you raised  
17   that point. I would like to get a clarification on  
18   that, if I may. I don't mean to interrupt your  
19   presentation, but since you raised it, Methanex-US  
20   did not, as it were, receive supplies at a depot in  
21   Texas and then tranship them to California. The

1 supplies were shipped directly from Medicine Hat to  
2 California?

3 MR. DUGAN: But I think they were shipped  
4 and may have been stored in inventory in  
5 California, in Methanex-US's inventory in  
6 California.

7 ARBITRATOR REISMAN: But they came  
8 directly from Canada as opposed to supplies that  
9 might have been produced in Fortier, which would  
10 have been sent from the U.S.--from Methanex  
11 investment in the United States which would have  
12 been sent directly to California. Do they--do the  
13 imports from Medicine Head qualify as investments  
14 just because you have a marketing center in Texas?

15 MR. DUGAN: Well, I think the way we  
16 approach the question is that Methanex-US, the  
17 distribution and marketing arm, is quite clearly an  
18 investment in the U.S. It has all the requisite  
19 properties needed to be an investment in the U.S.  
20 It has assets, real assets, and intangible assets.  
21 It has employees. It has income. It transfers the

1 income to its parent corporation.

2           There is no reason whatever to doubt that  
3 it is a very substantial company, and that's laid  
4 out in the Macdonald affidavit.

5           ARBITRATOR REISMAN: Yes, and I understand  
6 that, and that seems to be beyond any question.

7           MR. DUGAN: Right.

8           ARBITRATOR REISMAN: My question, to put  
9 it in more general terms, is where an investor  
10 establishes an investment, does that investment  
11 transform anything that it regularly effectively  
12 imports into the United States into an investment  
13 by some sort of association or affiliation?

14           MR. DUGAN: Well, I don't think it  
15 transforms the imports into an investment, and  
16 that's not our case. Our case is that Methanex-US  
17 is an ongoing concern. It's an ongoing operation  
18 with a going value--going-concern value. And that  
19 consists of not just its tangible assets such as  
20 its rail cars and its storage depots, but it's  
21 also--the assets of the corporation include its

1 customer base, its goodwill, its customer list, and  
2 its market share. And it was those assets of the  
3 investment that were damaged by the MTBE ban. It  
4 was the elimination of that market share--that list  
5 of customers, if you will--that damaged  
6 Methanex-US.

7           Now, again, it's an active operation, and  
8 if you had a situation where simply assets were  
9 coming--imports were coming straight into the  
10 country without any corresponding U.S. investment,  
11 to manage the sale and the distribution of those  
12 assets, it would be a much different situation, but  
13 obviously that's not what we are faced with here.

14           Now, the U.S. also makes the point that  
15 NAFTA--that Chapter 11 is not meant to apply to  
16 cross-border trade, but there had been a string of  
17 cases saying the various chapters of NAFTA are  
18 cumulative, and you could have a situation that  
19 involves both cross-border trade and investment,  
20 and I think that's precisely what the situation is  
21 here.

1           So long as Methanex meets the criteria for  
2 bringing a claim under Chapter 11, the fact that  
3 the original source of the products is Canada and  
4 not Fortier is irrelevant. If we can show a damage  
5 to our investment assets in the United States, then  
6 we meet the legal criteria for bringing a Chapter  
7 11 claim, and it's simply irrelevant where the  
8 assets originated from.

9           And if, indeed, Methanex has or Canada is  
10 entitled to protections under other Chapters of  
11 NAFTA for the cross-border trade, that is also  
12 irrelevant. The question here is whether  
13 Methanex-US, as a U.S. investment with real assets,  
14 both tangible and intangible in the United States  
15 has been damaged. If it has been, then it meets  
16 criteria for a Chapter 11 claim.

17           Now, I have actually got only about 10  
18 minutes, I think.

19           Now, one point I would like to make, I  
20 have spent a lot of time today in the opening  
21 pointing to what we think is one of the more

2007

1 significant--what is the most significant factor,  
2 and that is the shift to ethanol. That's Governor  
3 Davis's decision not just to ban MTBE, but to shift  
4 to ethanol.

5           His decision in the Executive Order in  
6 March 1999 to evaluate only ethanol, and  
7 Mr. Kenny's statement to Congress in October of  
8 1999, prior to the time that any evaluation was  
9 completed, that ethanol was going to be--was going  
10 to be, will be, I think is the phrase, substituted  
11 for MTBE because it's the only feasible oxygenate.

12           Now, we have made that point that there  
13 was this precipitous shift to MTBE without any  
14 environmental justification, without any rational  
15 justification whatsoever for quite a long time, and  
16 you know what Methanex's position is as to why they  
17 shifted so precipitously to ethanol. But I've  
18 never heard the U.S. response. I never heard the  
19 U.S. explain what it could possibly be meant by  
20 Mr. Kenny when he said in October of 1999 that  
21 ethanol was the only feasible alternative. We

1 never heard an explanation from the United States  
2 as to why Governor Davis selected only ethanol as  
3 an oxygenate to evaluate in March of 1999. And  
4 that's a very, very important point for our case.  
5 It's a very, very important piece of evidence.

6           And the United States has a habit of  
7 simply ignoring inconvenient and stubborn facts and  
8 then waiting to the last moment to come up with  
9 some purported justification for what really  
10 happened. We think, as a matter of the requirement  
11 of UNCITRAL for an opportunity, a fair opportunity,  
12 to present our case that if they come back tomorrow  
13 and try to explain why Mr. Kenny said in October of  
14 1999 that ethanol was the only feasible oxygenate,  
15 or if they come back tomorrow with some explanation  
16 as to why Governor Davis selected ethanol and only  
17 ethanol for evaluation in March 1999, that we  
18 should have a chance to respond to that, however  
19 briefly. We never heard their explanation, and we  
20 think we are entitled to respond to it, whatever it  
21 is.

1           Now, the last thing I would like to draw  
2 the Tribunal's attention to is the chart that the  
3 United States itself put up with respect to a  
4 statement of Mr. Macdonald, in which they said that  
5 this was somehow evidence of improper intent. We  
6 think that's virtually perverse. We think what it  
7 shows is something entirely the opposite.

8 Mr. Macdonald stated that a lot of the energy today  
9 in the U.S. is on energy security, and methanol has  
10 pounced on that, said Michael Bennett, senior vice  
11 president of technology for Methanex. The voice of  
12 methanol has not been heard in that debate, he  
13 said. Our strategy, as a company, was to get  
14 involved through an international trade dispute.

15           And then he goes on, and this is the  
16 important point: That's the only forum where we  
17 have an opportunity to even get a hearing, because  
18 the media and the rhetoric of the ethanol lobby had  
19 made it difficult for the facts to be heard, he  
20 said.

21           And that's precisely the point. Methanex

1 agreed to open this hearing--it didn't have to, and  
 2 it agreed to open this hearing--before there were  
 3 any rulings, before the FTC interpretation, because  
 4 I think it's important for this to be an open  
 5 hearing and for the facts to get out.

6           PRESIDENT VEEDER: But just don't forget  
 7 the point you might want to make. When this case  
 8 started, it wasn't intended to be an open hearing.

9           MR. DUGAN: That's my point, and we agreed  
 10 to open it up because we thought it important to be  
 11 aired publicly, the facts with respect to what  
 12 ethanol has done be heard publicly, and that is the  
 13 reason Methanex changed its position and agreed to  
 14 it.

15           But more importantly, and here is the key  
 16 to this: Methanex did not believe that it would  
 17 get a hearing, much less a fair hearing, in  
 18 California from Governor or Davis for all of the  
 19 obvious reasons that had been presented here.  
 20 Methanex did not believe it would get a fair  
 21 hearing from the United States Government. The

1 Federal Government itself created the ethanol  
2 industry with the Federal tax subsidy in 1977, and  
3 since then has continued the subsidies and put in  
4 place a whole range of programs designed to protect  
5 and cosset the ethanol industry, including, for  
6 example, the 54 percent gallon import duty.  
7 Methanex did not believe it could get a fair  
8 hearing from the Federal Government, either.

9           Methanex did believe it could get a fair  
10 hearing from a neutral international tribunal,  
11 where it could present the facts, it could present  
12 the law, and it could respectfully ask for a  
13 decision on the merits, independent of the  
14 political pressures that exist in California and in  
15 Washington, D.C., and that's why it brought this  
16 case to this Tribunal.

17           And that's what it asks for here: A fair  
18 hearing and a decision on the merits of case,  
19 independent of the politics of ethanol.

20           Thank you.

21           PRESIDENT VEEDER: Thank you very much,

1 Mr. Dugan.

2 Just before we wrap things up because we  
3 still have a little time, the matters on which you  
4 are going to come back to us, Mr. Dugan, was a  
5 package of the relevant California regulations, the  
6 three sets of regulations: the original, the  
7 proposed, the ones as they came into force.

8 MR. DUGAN: Right.

9 PRESIDENT VEEDER: And I think also in  
10 answer to my colleague, Mr. Rowley, you were going  
11 to come back with some answers regarding political  
12 contributions.

13 MR. DUGAN: Right. I think I could answer  
14 that now, actually.

15 And this is--I'm citing footnote 78 from  
16 the U.S. rejoinder, and I have no reason to believe  
17 this is not true. Methanex Management,  
18 Incorporated, a subsidiary of Methanex Corporation,  
19 made a \$10,000 donation to the Democratic National  
20 Committee and a \$15,000 donation to the Republican  
21 National State Elections Committee one week apart.

1 They were returned, even though Methanex  
 2 Management, Inc., a U.S. couple, I believe, because  
 3 they were drawn on a Canadian bank. Thereafter,  
 4 Methanex has made no more contributions to the--any  
 5 politician in the United States and has a corporate  
 6 policy against it.

7 And we are going to get the cases to the  
 8 United States tonight. I assume you would like  
 9 them by E-mail?

10 MR. LEGUM: That's okay.

11 PRESIDENT VEEDER: Could we go through as  
 12 housekeeping matters certain matters which we need  
 13 to address. You're still pursuing your application  
 14 to maintain the three exhibits which you adduced in  
 15 evidence in response to the amici submissions.  
 16 These are Tabs 3, 13, and 14 of volume one to your  
 17 response to the amici submissions which were  
 18 opposed by the United States. If you have anything  
 19 to say further beyond your written submissions on  
 20 that, we would gladly hear you.

21 MR. DUGAN: I do not.

1           PRESIDENT VEEDER: In regard to your  
2 motion regarding the travaux, we have asked you  
3 some questions and you have done your best to  
4 answer them. Do you need any more time to  
5 elaborate on your answers further?

6           MR. DUGAN: No, we do not.

7           PRESIDENT VEEDER: Canada and Mexico have  
8 not yet intimated they want to address us orally at  
9 this hearing, but they have intimated that they  
10 would like to put in possibly further written  
11 submissions under Article 1128 after this hearing.  
12 If they did so, would you be minded to want an  
13 opportunity to respond to those written  
14 submissions?

15          MR. DUGAN: We would like an opportunity  
16 to respond. I'm not sure that we will, but we  
17 would like an opportunity to respond, number one.

18          But number two, I would like--the  
19 signatories have had a tendency to comment on  
20 factual matters in the case. I believe that the  
21 Article gives them the right to comment on the

1 interpretation only, and we would request the  
2 direction from the Tribunal that if they are going  
3 to comment that their comments be limited to an  
4 interpretation of the Treaty itself.

5           PRESIDENT VEEDER: Next, although the  
6 transcript has been splendidly produced and  
7 prepared, there are occasional mistakes which we  
8 can see. What we have in mind and will address  
9 this tomorrow with both parties is a procedure for  
10 correcting any significant errors. We are not  
11 concerned with obvious errors or minor matters, but  
12 we would want a fairly prompt timetable for  
13 notifying errors between the parties and agreeing,  
14 where they can, certain corrections; and where they  
15 can't agree, parties can notify us with respective  
16 corrections. But we will come back to that  
17 tomorrow, if you could think about your position  
18 about that.

19           The other matter is costs which you  
20 touched on. We need some information about costs  
21 from both parties, and what we are minded to do is

1 asking for the parties in a fairly short order to  
2 produce their respective figures broken down at  
3 least in part with any submissions in support of  
4 the quantum of costs to date. And we also  
5 envisaged there would be an opportunity for each  
6 party, disputing party, to comment on the other  
7 side's figures. So, we need to build that  
8 timetable into the future program after this  
9 hearing.

10           Subject to that, unless anybody has  
11 something to raise now, we will adjourn until 2:30  
12 tomorrow afternoon, anticipating that we shall  
13 finish by seven that evening.

14           MR. LEGUM: That sounds very good, but  
15 there is one matter that the United States will  
16 raise tomorrow at the close of the hearing, and I  
17 might as well provide advanced notice so everyone  
18 has a chance to think about it, and that is that we  
19 will request the Tribunal to enter an order closing  
20 the proceedings subject to further order from the  
21 Tribunal. I think after the last hearing there

1 were a succession of posthearing submissions and it  
 2 would be best if we maintain--if the Tribunal  
 3 maintained control over further submissions that  
 4 were received.

5 PRESIDENT VEEDER: You have in mind  
 6 Article 29 of the UNCITRAL Rules?

7 MR. LEGUM: Yes.

8 PRESIDENT VEEDER: We'll come to that,  
 9 certainly.

10 MR. DUGAN: I would just like to note that  
 11 what I think you're referring to is the issuance of  
 12 the FTC interpretation that came after the close of  
 13 this jurisdictional phase, and that's what  
 14 triggered the back and forth. And I would like to  
 15 reserve for the record our right to respond to any  
 16 purported interpretation issued by the FTC.

17 PRESIDENT VEEDER: Mr. Dugan, you are  
 18 quite right. That's what Mr. Legum had in mind,  
 19 but we could address that tomorrow.

20 Of course, it's not a complete closure.  
 21 The Tribunal always has the right to reopen, having

1 closed the hearing to the parties under Article  
2 29(2).

3 But if that's all, we will stop here.

4 Thank you very much, Mr. Dugan. And we will start  
5 again tomorrow at 2:30.

6 (Whereupon, at 6:40 p.m., the hearing was  
7 adjourned until 2:30 p.m. the following day.)

8

9

10

11

12

13

14

15

16

17

18

19

20

21

1 CERTIFICATE OF REPORTER

2

3 I, David A. Kasdan, RDR-CRR, Court

4 Reporter, do hereby testify that the foregoing

5 proceedings were stenographically recorded by me

6 and thereafter reduced to typewritten form by

7 computer-assisted transcription under my direction

8 and supervision; and that the foregoing transcript

9 is a true record and accurate record of the

10 proceedings.

11 I further certify that I am neither

12 counsel for, related to, nor employed by any of the

13 parties to this action in this proceeding, nor

14 financially or otherwise interested in the outcome

15 of this litigation.

16

17 DAVID A. KASDAN, RDR-CRR

18

19

20

21

